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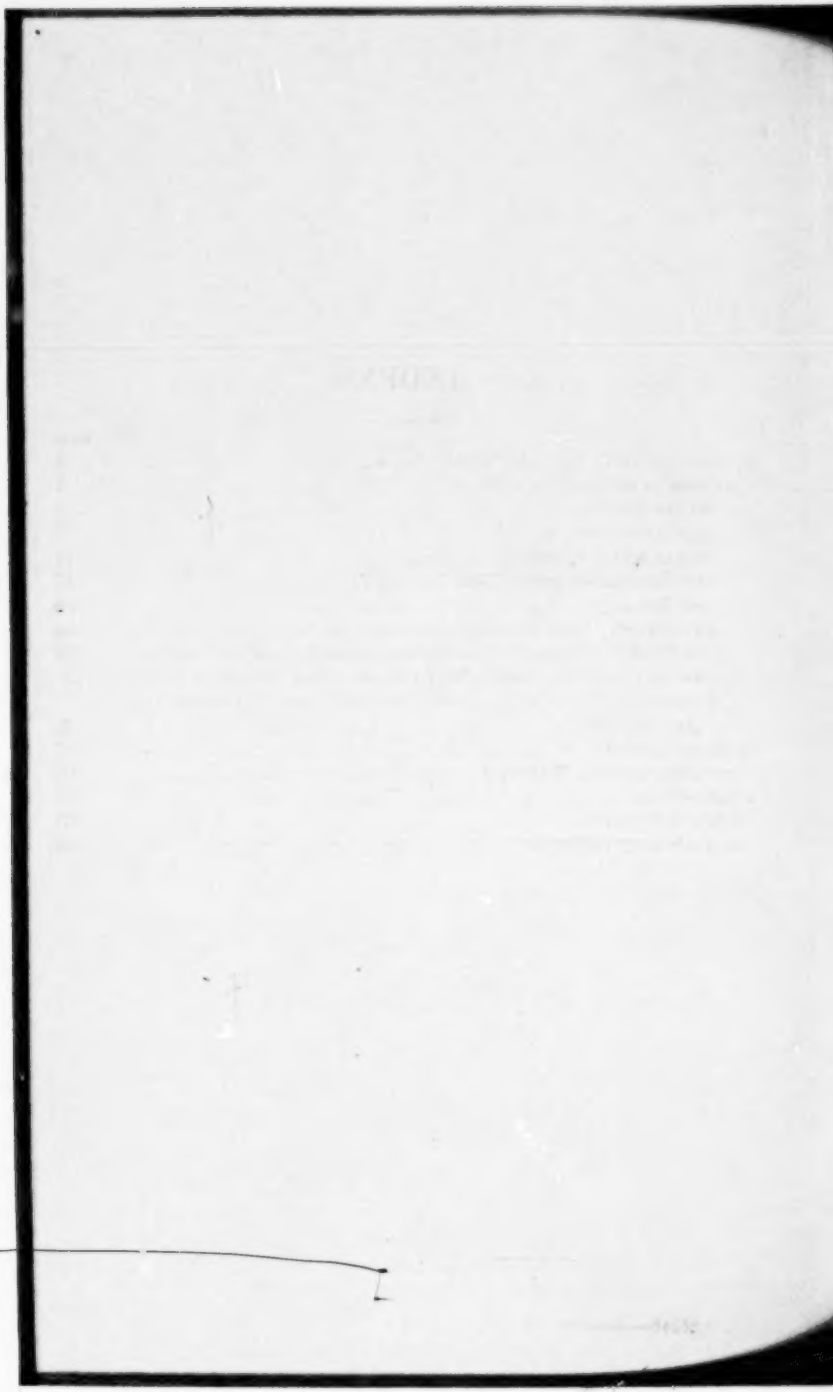

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APPENDIX TO THE PETITIONER'S BRIEF

Docket Entries

Docket No. 9893

Philadelphia Transportation Company, petitioner

v.

Commissioner of Internal Revenue, respondent

Appearances: For petitioner—William R. Spofford, Esq., Frederic L. Ballard, Esq., Chester J. McGuire, Esq., Sherwin T. McDowell, Esq. For respondent: Brooks Fullerton, Esq.

DOCKET ENTRIES

1945

Dec. 27—Petition received and filed. Taxpayer notified. Fee paid.

Dec. 27—Request for hearing at Philadelphia, filed by taxpayer. 1/9/46 Granted.

1946

Jan. 2—Copy of petition served on General Counsel.

Feb. 27—Answer filed by General Counsel.

Mar. 5—Copy of answer served on taxpayer—Philadelphia, Pennsylvania.

1947

Jan. 20—Hearing set March 17, 1947—Philadelphia, Pennsylvania.

Mar. 17—Hearing had before Judge Harlan on merits. Motion to file amendment to petition—Granted; Motion and amendment to petition; answer to amendment to petition and appearance of Sherwin T. McDowell as counsel filed. Stipulation of facts and supplemental stipulation of facts also filed at hearing. Copy of motion and amendment served. Petitioner's brief due 4/16/47. Respondent's brief 5/16/47. Respondent's reply brief 6/5/47.

Apr. 1—Transcript of hearing 3/17/47 filed.

Apr. 16—Brief filed by taxpayer. 4/16/47 Copy served.

1947

May 7—Motion for extension to 6/16/47 to file brief, brief lodged, filed by General Counsel. 5/8/47 Granted.

July 11—Motion for extension to file the attached brief, brief lodged, filed by General Counsel. 7/15/47 Granted.

Aug. 5—Motion for extension to 8/20/47 to file reply brief, filed by taxpayer. 8/7/47 Granted.

Aug. 20—Reply brief filed by taxpayer. Copy served.

Nov. 28—Findings of fact and opinion rendered, Judge Harlan. Decision will be entered under Rule 50. 12/3/47 Copy served.

1948

Feb. 17—Respondent's computation for entry of decision filed. Agreed to.

Feb. 19—Decision entered. Judge Harlan. Div. 11.

May 17—Petition for review by U. S. Circuit Court of Appeals, 3rd Circuit, filed by General Counsel.

May 17—Notice of filing petition for review sent to W. R. Spofford, filed.

May 19—Proof of service of petition for review on W. R. Spofford filed.

May 20—Proof of service of petition for review on taxpayer filed.

June 9—Motion for extension to 8/13/48 for the parties to file their stipulation re record, filed by General Counsel.

July 9—Order enlarging time to 8/13/48 to prepare and transmit record, entered.

Aug. 5—Motion to retain exhibits in Clerk's office until ten days prior to hearing in the U. S. Circuit Court of Appeals, 3rd Circuit, filed by General Counsel. 8/6/48 Motion Granted.

Aug. 5—Stipulation re record on review filed.

The Tax Court of the United States

Docket No. 9893

PHILADELPHIA TRANSPORTATION COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

STIPULATION OF FACTS

It is hereby stipulated with respect to the above-entitled proceeding that the following statements may be accepted as facts and that this stipulation shall be without prejudice to the right of either party to introduce other and further evidence at the trial of this case not inconsistent with the facts herein stipulated.

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1. Philadelphia Transportation Company (hereinafter referred to as petitioner) is a corporation organized under the laws of the Commonwealth of Pennsylvania, with its office and principal place of business at 1405 Locust Street, Philadelphia, Pennsylvania.

2. Petitioner keeps its books of accounts and files its tax returns on the accrual basis of accounting.

3. Petitioner's consolidated Federal income and Declared Value Excess Profits Tax Return for the calendar year 1942 was filed with the Collector of Internal Revenue for the First Collection District of Pennsylvania at Philadelphia, Pennsylvania, on June 15, 1943, pursuant to an extension to June 15, 1943, of time for filing duly granted by respondent on May 7, 1943. Photostatic copy of the petitioner's consolidated Federal Income and Declared Value Excess Profits Tax Return for the calendar year 1942 is submitted herewith, made a part hereof and marked Exhibit 1-A.

4. In its consolidated Federal Income and Declared Value Excess Profits Tax Return for the calendar year 1942 petitioner reported taxable net income (i. e. "normal tax net income") in the amount of $1,780,269.13 and liability for income tax in the amount of $747,517.96 which was paid. Respondent, in his Notice of Deficiency, mailed to petitioner on October 8, 1945 (Exhibit A of the petition) determined an income tax deficiency against petitioner in the amount of $834,982.38.

5. On October 23, 1945, petitioner paid to the Collector of Internal Revenue, Philadelphia, Pennsylvania, $925,052.05 of which $800,000 was in partial payment of the deficiency determined by respondent and $125,052.05 was interest on such $800,000 from March 15, 1943, to October 23, 1945. A transcript from the Collector's records evidencing the payments on account of income tax for 1942 is submitted herewith, made a part hereof and marked Exhibit 2–B.

6. On October 1, 1934, Philadelphia Rapid Transit Company, a corporation organized under the laws of the Commonwealth of Pennsylvania, filed in the District Court of the United States for the Eastern District of Pennsylvania, a petition under Section 77B of the Bankruptcy Act. Philadelphia Rapid Transit Company operated as lessee under long-term leases properties of sixty-four other corporations, twenty-seven of which filed petitions as additional debtors for reorganization under the 77B proceedings. These twenty-seven corporations are listed on page 2 of the "Plan," Exhibit 3–C *infra,* and are referred to therein and herein as "Lessor Companies." The Philadelphia Rapid Transit Company, its subsidiaries and the "Lessor Companies" were referred to throughout the reorganization proceedings as The Philadelphia Rapid Transit Company System. Neither the Philadelphia Rapid Transit Company nor its subsidiaries (listed on Schedules "A" and "B", pages 15 and 16 of the "Plan") owned stock of the twenty-seven "Lessor Companies."

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7. On December 1, 1934, a "Plan of Reorganization of Philadelphia Rapid Transit Company System" was filed. On April 1, 1937, a "Revised Plan of Reorganization of Philadelphia Rapid Transit Company System" was filed. Neither of these Plans was approved and confirmed by the Court.

8. On December 1, 1937, a "Second Revised Plan of Reorganization of Philadelphia Rapid Transit Company System" was filed. Amendments to this "Plan" were filed on June 1, 1938, and on November 15, 1938. The "Second Revised Plan" as amended is herein called the "Plan." A copy of the "Plan" is submitted herewith, made a part hereof and marked Exhibit 3–C.

9. The "Plan" provided for the consolidation and merger of sixty-five of the corporations previously constituting the Philadelphia Rapid Transit Company System. Pursuant to the "Plan" an "Agreement of Consolidation and Merger" was adopted by said sixty-five corporations. A copy of said "Agreement of Consolidation and Merger" is submitted herewith, made a part hereof and marked Exhibit 4–D.

10. The "Plan" was approved and confirmed by the Court on November 14, 1939. A copy of the order of the Court entered November 14, 1939, confirming the "Plan" is submitted herewith, made a part hereof and marked Exhibit 5–E.

11. The "Plan" provided that petitioner, upon incorporation, would issue to holders of stock and stock trust certificates of twenty-one of said "Lessor Com-

panies,"[1] petitioner's 3%–6% Consolidated Mortgage Bonds in the amount of $31,973,597.78 and to holders of First Mortgage Bonds of two of said "Lessor Companies," petitioner's 3%–6% Consolidated Mortgage Bonds in the amount of $596,400.00. $200,000 of the $596,400 face amount 3%–6% Consolidated Mortgage Bonds were issued to holders of Doylestown and Willow Grove Railway Company First Mortgage 4% Bonds in exchange for $500,000 face amount of said bonds and the remaining $396,400 face amount were issued to holders of Darby, Media and Chester Street Railway Company 4½% First Mortgage Bonds in exchange for $991,000 face amount of said bonds. (See pages 8 and 20 of the Plan.")

12. Semi-annual interest in the amount of $10,000.00 due June 1, 1939, on the Doylestown and Willow Grove Railway Company 1st Mortgage 4% bonds of the face value of $500,000.00 was paid on or about July 30, 1939. "Fixed Interest Coupon No. 1" on the $200,000 face amount of 3%–6% Consolidated Mortgage Bonds exchanged for said $500,000 bonds was removed before delivery. Interest in the amount of $500 for the period from June 1, 1939, to July 1, 1939, was paid by petitioner at the rate of 3% on $200,000 on January 29, 1940.

13. Semi-annual interest in the amount of $22,297.50 due July 1, 1939, on the Darby, Media and Chester Street Railway Company 4½% First Mort-

[1] These "Lessor Companies" are listed on page 18 of the "Plan." Electric Traction Company and Peoples Traction Company appear on the list as "Electric & Peoples Traction."

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gage Bonds of the face value of $991,000 was paid on or about July 30, 1939. "Fixed Interest Coupon No. 1" on the $396,400 face amount of 3%–6% Consolidated Mortgage Bonds exchanged for said $991,000 bonds was removed before delivery.

14. In accordance with the "Plan" and as a result of said "Agreement of Consolidation and Merger" petitioner came into existence as a corporation on January 1, 1940, immediately after midnight, December 31, 1939.

15. Because of the operation during 1939 of the sinking fund for Peoples Passenger Railway Company stock trust certificates, the amount of $31,973,597.78 of bonds (Schedule D of the "Plan" which is Exhibit 3–C hereof) was reduced to $31,933,543.54 (total of face value of 3%–6% Consolidated Mortgage Bonds on Exhibit "A" of "Agreement of Consolidation and Merger" which is Exhibit 4–D hereof).

16. On January 29, 1940, petitioner, pursuant to said "Plan" executed and delivered its 3%–6% Consolidated Mortgage Bonds in the amount of $32,529,943.54,[2] dated January 1, 1939, and bearing interest from January 1, 1939,[3] to the Fidelity-Philadelphia

[2] For an explanation of the issuance of additional 3%–6% Consolidated Mortgage Bonds in the amount of $11,810,100, see the second footnote on page 20 of the "Plan" (Exhibit 3–C). No interest was paid on these bonds.

[3] Except that in the case of the $596,400 principal amount of said bond referred to in paragraphs 12 and 13 *supra* "Fixed Interest Coupon No. 1" was removed.

Trust Company, then and now Trustee for the bondholders, for authentication. The Trustee forthwith authenticated the bonds and delivered them to Drexel & Co., depositary, for delivery to the persons and in the amounts mentioned in paragraph 11 *supra*. A "Specimen" bond of such issue is submitted herewith, made a part hereof and marked Exhibit 6–F.

17. Said bonds were secured by a mortgage upon all of the properties of the petitioner, subject only to the prior encumbrances listed in Schedules E–1, E–2, E–3 and E–4 of the "Plan" (Exhibit 3–C). Said mortgage was executed and delivered by the petitioner on January 4, 1940, and recorded in Philadelphia County, Pennsylvania, on January 9, 1940, in Delaware County, Pennsylvania, on January 10, 1940, in Bucks County, Pennsylvania, on January 11, 1940, and in Montgomery County, Pennsylvania, on January 11, 1940. A copy of said Trust Indenture is submitted herewith, made a part hereof, and marked Exhibit 7–G.

18. A copy of the balance sheet with which petitioner opened its books in the late Spring of 1940 as of January 1, 1940, is submitted herewith, made a part hereof and marked Exhibit 8–H. The item listed under "Liabilities" on said balance sheet and designated as:

Matured interest and rents unpaid	$906,702.47

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was made up of items appearing on petitioner's books as follows:

Philadelphia Rapid Transit Co., dividends payable	$1,257.50
Lessor Co. dividends payable	2,406.87
Payment of rent for use of underliers' property due their stockholders	3,353.74
Drexel & Co. Agent—Exchange of Doylestown & Willow Grove Ry. Co. 1st Mtge. bonds [see paragraph 12, *supra*]	500.00
Drexel & Co. Agent—Exchange of Lessor Cos.' bonds for Philadelphia Transportation Co. 1st & Ref. 4% bonds	22,172.06
Fidelity-Philadelphia Trust Co.—Fixed interest for 1939 on issue of Philadelphia Transportation Co. 3%–6% consolidated mortgage bonds Series A	[1] 966,952.30
Total	996,702.47

[1] This sum was computed as follows:

3% ("Fixed Interest Coupons No. 1 and No. 2") on $31,933,543.54 bonds issued to stockholders of twenty-one "Lessor Companies" (See paragraphs 11 and 15, *supra*)	$958,006.30
1.5% ("Fixed Interest Coupon No. 2") on $596,400 bonds issued to bondholders of two "Lessor Companies" (see paragraphs 11, 12, and 13, *supra*)	8,946.00
	966,952.30

19. On January 29, 1940, petitioner delivered its check in the amount of $977,112.00 to the Trustee for bondholders of said 3%–6% Consolidated Mortgage Bonds with direction to the Trustees to pay to the bondholders an amount equivalent to 3% of the face amount of their respective bonds upon surrender for redemption of coupons numbered 1 and 2 affixed to said bonds which coupons were designated in the trust indenture as "Fixed Interest Coupons." This transaction was recorded on the books of petitioner by a debit of $977,112.00 against the liability shown on

the opening balance sheet (supplemented by adjusting credits not here material) as follows:

1940		
Jan. 1—Opening balance sheet (see par. 18)		$968,952.30
Jan. 29—Check to trustee	$977,112.00	
Jan. 31—Refund		7,794.00
May 17—Refund		1,212.00
Aug. 29—Refund		954.00
Aug. 31—Journal entry		199.70
	977,112.00	977,112.00

20. The item listed under "Liabilities" on the balance sheet with which petitioner opened its books as of January 1, 1940 (Exhibit 8–H) and designated as "Accrued Interest and Rent, Payable, $1,629,979.39", was made up of items appearing on Petitioner's books as follows:

Accrued interest on funded debt	$321,640.91
Accrued interest on unfunded debt	1,073.34
Accrued rents—City of Phila. Lines	474,579.37
Accrued rent—Delaware River Bridge Line	11,535.05
Accrued miscellaneous debits	925.54
Income interest on Phila. Transportation Co. consolidated 3%-6% bonds	820,225.18
	1,629,979.39

21. The item appearing in paragraph 20 as "Income Interest on Phila. Transportation Co. Consolidated 3%–6% Bonds $820,225.18" constituted the variable payment on said bonds required to be made on July 1, 1940. It was computed at the rate of 2.52% on $32,529,943.54 face amount of outstanding bonds in accordance with a report made to petitioner by Lybrand, Ross Bros. and Montgomery, Certified Public Accountants, dated April 29, 1940. A copy of said report is submitted herewith, made a part hereof and marked Exhibit 9–I. Rentals payable by Philadelphia Rapid Transit Company to the "Lessor Companies"

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for 1939 in the amount of $7,470,817,80 and an ad interim payment of $700,000 paid to certain "Lessor Companies" in 1939 in connection with the reorganization proceedings and pursuant to an order of the Federal District Court having jurisdiction thereof, are not reflected in said report.

22. On June 28, 1940 petitioner delivered its check in the amount of $819,754.58 to the Trustee for bondholders of said 3%–6% Consolidated Mortgage Bonds with direction to the Trustee to pay to the bondholders an amount equivalent to 2.52% of the face amount of their respective bonds upon surrender for redemption of coupon Number 1 affixed to said bonds which coupon was designated in the trust indenture as "Income Interest Coupon". This transaction was recorded on the books of petitioner by a debit of $819,754.58 against the liability of $820,225.18 shown on the opening balance sheet. Said sum was paid to the bondholders on July 1, 1940.

23. In accordance with regulations of the Public Utilities Commission of the Commonwealth of Pennsylvania, said payments of $966,952.30, $500.00 (see paragraph 12, *supra*) and $819,754.58 were not charged as an expense in petitioner's accounts for 1940.

24. Petitioner accrued on its books in 1940 the fixed and income interest payments due with respect to said 3%–6% Consolidated Mortgage Bonds and payable as follows:

Fixed interest (coupon 3)	July 1, 1940
Fixed interest (coupon 4)	Jan. 1, 1941
Income interest (coupon 2)	July 1, 1941

It deducted these amounts on its tax return for the year 1940 as interest and Respondent has allowed said deductions. These deductions are not in issue in this proceeding.

25. On its Corporation Income and Declared Value Excess Profits Tax Return for 1940 (Schedule 1-A "Reconciliation of Net Income Year Ending December 31, 1940") petitioner, among other items, subtracted the sum of $1,787,206.88 designated "Payment on Philadelphia Transportation Co. 3%-6% Consolidated Mortgage Bonds Schedule 12" from "Income per books" to arrive at "Net Income [Loss] per Tax Return." Photostatic copy of the petitioner's Consolidated Federal Income and Declared Value Excess Profits Tax Return for the calendar year 1940 is submitted herewith, made a part hereof and marked Exhibit 10-J.

26. On its Federal Income Tax Return for the calendar year 1940 petitioner claimed as a deduction $1,787,206.88 ($967,452.30[4] paid in January 1940 plus $819,754.58 paid in July 1940) as interest paid in computing its 1940 taxable income [loss].

27. Petitioner's consolidated Income and Declared Value Excess Profits Tax Return for the calendar year 1940 was filed on July 22, 1941 pursuant to an extension to August 15, 1941, of time for filing duly granted by the respondent on June 4, 1941. No waivers or extensions of the period for assessment were ever filed.

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[4] This amount consists of the $966,952.30 referred to in paragraphs 18 and 19, *supra*, and the $500 referred to in paragraph 12, *supra*.

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28. Photostatic copy of petitioner's consolidated Federal Income and Declared Value Excess Profits Tax Return for the calendar year 1941 is submitted herewith, made a part hereof and marked Exhibit 11-K.

29. In determining petitioner's net operating loss deduction for 1942 respondent disallowed the item of $1,787,206.88, claimed as a deduction on the return and referred to in paragraph 26 in computing the net operating loss for 1940 to be carried over to 1942.

30. In the event that it shall be finally determined that petitioner is entitled to carry forward a larger net operating loss from 1940 than that allowed by Respondent, petitioner is entitled to an increase in net operating loss deduction for 1942 to the same extent.

31. Respondent concedes that petitioner is entitled to additional deductions for ordinary and necessary business expenses for the years 1940 and 1941 as follows:

1940	$10,817.21
1941	13,227.42

Respondent concedes that by virtue of the allowance of such additional ordinary and necessary business expenses, petitioner is entitled to an increase in the net operating loss deduction for 1942 in the amount of $24,044.63.

32. Respondent concedes that by virtue of petitioner's duly filed election to accelerate the amortization of certain emergency facilities petitioner is entitled to an additional deduction in the year 1942 for amortization of such facilities in the amount of $7,435.00. The petitioner concedes that by reason of

said additional deduction for said amortization in the amount of $7,435.00, the deduction for Pennsylvania corporate net income tax as allowed in the deficiency notice should be reduced by $290.08.

33. The indebtedness incurred by petitioner and evidenced by said 3%–6% Consolidated Mortgage Bonds was not incurred or continued to purchase or carry obligations the interest upon which is wholly exempt from tax under Chapter 1, Sub-title A of the Internal Revenue Code.

W. R. Spofford,
WILLIAM R. SPOFFORD,
Counsel for Petitioner,
J. P. WENCHEL,
Chief Counsel,
Bureau of Internal Revenue.

The Tax Court of the United States

Docket No. 9893

PHILADELPHIA TRANSPORTATION COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

SUPPLEMENTAL STIPULATION OF FACTS

It is hereby stipulated with respect to the above-entitled proceeding that if the Consolidated Income and Excess Profits Tax Return of Philadelphia Rapid Transit Company for the calendar year 1939 is received in evidence (over objection of petitioner), the following statements may be accepted as facts.

1. Schedule No. 3 of said return is the "Philadelphia Rapid Transit System [Company] Consoli-

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dated Balance Sheet as of December 31, 1938" and "as of December 31, 1939." Under "Liabilities-Accounts Payable and Current Liabilities" on said balance sheet as of December 31, 1938, the item of $37,188,067.74 includes $28,692,245.94 accrued and unpaid rentals due the "Lessor Companies" mentioned in the principal Stipulation of Facts in this proceeding. Under "Liabilities-Accounts Payable and Current Liabilities" on said balance sheet as of December 31, 1939, the item $43,708,918.32 includes $35,463,063.74 accrued and unpaid rentals due said "Lessor Companies."

2. Upon audit of the Consolidated Income and Excess Profits Tax Return of Philadelphia Rapid Transit Company for the calendar year 1939, the Internal Revenue Agent (Mr. Charles Quinn) making such audit proposed to include certain items of additional income and disallow certain deductions claimed, which if sustained would have resulted in a deficiency of income and excess profits taxes of $190,558.26.

3. Among the items claimed as deductions, Revenue Agent Quinn proposed to disallow accrued rentals for the year 1939 payable by Philadelphia Rapid Transit Company to the "Lessor Companies" (referred to and described in the principal Stipulation) in the amount of $6,970,577.60. Said "Lessor Companies" kept their books of accounts and filed their tax returns on the cash receipts basis of accounting.

4. Subsequently, Mr. Quinn died before his recommendations were reviewed and the matter was assigned to Revenue Agent McLarren.

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5. Thereafter, conferences were held by representatives of the petitioner with representative of the respondent in which petitioner claimed a deduction for depreciation in excess of that claimed on the original return of Philadelphia Rapid Transit Company.

6. A copy of Revenue Agent McLarren's report to the Revenue Agent in Charge at Philadelphia, Pennsylvania is attached hereto, made a part hereof, and marked "Exhibit 12–L." The consolidated net income of $1,155,152.09 mentioned in said report is the net income as computed by Revenue Agent Quinn and results from his recommendation of the adjustments referred to in paragraph 2.

7. A copy of a letter dated May 29, 1941, sent to and received by the Philadelphia Rapid Transit Company in respect of the examination of its 1938 and 1939 income-tax returns is attached hereto, made a part hereof, and marked "Exhibit 13–M."

8. A copy of a letter dated August 21, 1941, sent by the Internal Revenue Agent in Charge to the Commissioner of Internal Revenue in respect of the 1938 and 1939 income-tax liability of Philadelphia Rapid Transit Company and related corporations is attached hereto, made a part hereof, and marked "Exhibit 14–N." No copy of this letter was furnished to petitioner.

William R. Spofford,
WILLIAM R. SPOFFORD,
Counsel for Petitioner,
J. P. WENCHEL,
Chief Counsel,
Bureau of Internal Revenue.

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Findings of Fact and Opinion

The Tax Court of the United States

Philadelphia Transportation Company, petitioner

v.

Commissioner of Internal Revenue, respondent

Docket No. 9863. Promulgated November 28, 1947

A plan of reorganization under section 77–B of the Bankruptcy Act, approved November 14, 1939, provided for merger and consolidation of 65 companies previously constituting the Philadelphia Rapid Transit Co. System into a new company to be incorporated, the petitioner herein. It also provided that the new company, upon incorporation, should issue to holders of stock and stock trust certificates of certain of the merged companies, its 3 per cent–6 per cent consolidated mortgage bonds dated January 1, 1939, and bearing interest from that date. Petitioner's corporate existence began on January 1, 1940. On January 29, 1940, it issued and delivered its 3 per cent–6 per cent bonds as provided in the plan, and in January and July of 1940 made the interest payments called for by the bonds for the year 1939. These payments, aggregating $1,787,206.88, were deducted as interest in petitioner's 1940 return. Its books were kept and its returns made on an accrual basis. *Held*, petitioner was entitled to accrue and deduct from gross income for 1940, as interest, the amount which under the provisions of its bonds issued in that year it was obligated to pay and did pay as interest for the period January 1 to December 31, 1939. *Columbia River Paper Mills*, 43 B. T. A. 104; affd., 126 Fed. (2d) 1009; *Oregon Pulp & Paper Co.*, 47 B. T. A. 722; *Ernst Kern Co.*, 1 T. C. 249; and *Pressed Steel Car Co.* v. *Commissioner*, 152 Fed. (2d) 280, followed.

W. R. Spofford, Esq., Frederick L. Ballard, Esq., and *Sherwin T. McDowell, Esq.,* for the petitioner.

Brooks Fullerton, Esq., for the respondent.

The respondent determined a deficiency in the income tax of petitioner for the calendar year 1942 in the amount of $834,982.38. The sole issue presented for our consideration is whether the petitioner, in

computing the statutory "net operating loss deduction" for the year 1942, may deduct from gross income for 1940 amounts paid by it in that year in redemption of interest coupons for 1939 on its 3 per cent–6 per cent consolidated mortgage bonds. The parties have agreed upon other issues, and their agreement will be given effect upon settlement under Rule 50.

The evidence consists of a stipulation and supplemental stipulation of facts and certain documents introduced at the hearing.

FINDINGS OF FACTS

The facts as stipulated are so found.

Philadelphia Transportation Co. (hereinafter referred to as petitioner) is a Pennsylvania corporation, with office and principal place of business in Philadelphia, Pennsylvania. It keeps its books and files its tax returns on the accrual basis of accounting.

Petitioner's consolidated Federal income and declared value excess profits tax return for the calendar year 1942 was filed with the collector of internal revenue for the first collection district of Pennsylvania at Philadelphia on June 15, 1943, pursuant to an extension to June 15, 1943, of time for filing duly granted by respondent on May 7, 1943. In that return petitioner reported taxable net income (i. e., "normal tax net income") in the amount of $1,780,269.13 and liability for income tax in the amount of $747,517.96, which was paid.

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On October 23, 1945, petitioner paid to the collector of internal revenue at Philadelphia $925,052.05, of which $800,000 was in partial payment of the deficiency determined by respondent and $125,052.05 was interest on the $800,000 from March 15, 1943, to October 23, 1945. In its petition, filed December 27, 1945, petitioner claims a refund of taxes and interest paid, together with interest thereon as provided by statute.

On October 1, 1934, the Philadelphia Rapid Transit Co. (one of the petitioner's predecessors), a Pennsylvania corporation, operated a street railway system in Philadelphia. On October 1, 1934, it filed a voluntary petition under section 77–B of the Bankruptcy Act in the district court of the United States for the eastern district of Pennsylvania. It operated, as lessee under long term leases, properties of 64 other corporations, 27 of which filed petitions as additional debtors for reorganization under the 77–B proceedings. These 27 corporations are referred to in the reorganization "Plan" and herein as "Lessor Companies." The Philadelphia Rapid Transit Co., its subsidiaries and the "Lessor Companies" were referred to throughout the reorganization proceedings as "The Philadelphia Rapid Transit Company System." Neither the Philadelphia Rapid Transit Co. nor its subsidiaries owned stock of the 27 "Lessor Companies."

A plan known as the "Second Revised Plan of Reorganization," hereinafter called the "plan," was filed on December 1, 1937, and amended on June 1 and November 15, 1938, and approved on November 14, 1939.

Page 1 of the plan contains the following statement:

> * * * The public holders of stock and stock trust certificates of Lessor Companies will receive in exchange for their present securities, approximately $31,974,000 face amount of 3%–6% Consolidated Mortgage Bonds and approximately $12,301,000 par value of Participating Preferred Stock (of a par value of $20 per share) of Transportation Company and approximately $2,204,000 in cash, as hereinafter set forth. The total fixed annual interest (3%) on the said new bonds will be approximately $6,141,000 less, and the total maximum interest payable if earned (6%) on the said new bonds will be approximately $5,182,000 less, than the annual rentals formerly paid to the holders of such securities of Lessor Companies under the old leases.

The plan provided that petitioner, upon incorporation, would issue to holders of stock and stock trust certificates of 21 of the "Lessor Companies" petitioner's 3 percent-6 percent consolidated mortgage bonds, dated January 1, 1939, and bearing interest from that date, in the amount of $31,973,597.78[1] and to holders of first mortgage bonds of two of the "Lessor Companies" petitioner's 3 percent-6 percent consolidated mortgage bonds in the amount of $596,400. The 3 percent-6 percent consolidated mortgage bonds were to bear "Fixed Interest" of 3 percent per annum and an "additional 3 percent per annum only if and to the extent to which earned in any

[1] Later decreased to $31,933,543.54.

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year." The $596,400 face amount of 3 percent-6 percent consolidated bonds were to be, and were, in January 1940, issued as follows: $200,000 of said amount to holders of Doylestown and Willow Grove Railway Co. first mortgage 4-percent bonds in exchange for $500,000 face amount of said bonds and the remaining $396,400 face amount to holders of Darby, Media & Chester Railway Co. 4½-percent first-mortgage bonds in exchange for $991,000 face amount of said bonds. Semiannual interest in the amount of $10,000 due June 1, 1939, on the Doylestown & Willow Grove Railway Co. first-mortgage 4-percent bonds of the face value of $500,000 was paid by the trustees of the "Debtor" on or about July 30, 1939. "Fixed Interest Coupon No. 1" on the $200,000 face amount of 3 percent-6 percent consolidated mortgage bonds exchanged for said $500,000 bonds was removed before delivery. Interest in the amount of $500 for the period from June 1 to July 1, 1939, was on January 29, 1940, paid in cash by petitioner at the rate of 3 percent on $200,000. Semiannual interest in the amount of $22,297.50 due, July 1, 1939, on the Darby, Media & Chester Street Railway Co. 4½-percent first-mortgage bonds of the face value of $991,000 was paid by the trustees of the "Debtor" on or about July 30, 1939. "Fixed Interest Coupon No. 1" on the $396,400 face amount of 3 percent-6 percent consolidated mortgage bonds exchanged for said $991,000 bonds was removed before delivery.

The plan also provided for the consolidation and merger of 65 of the corporations previously constituting the Philadelphia Rapid Transit Co. System.

Pursuant to the plan, an "Agreement of Consolidation and Merger" was adopted by the 65 corporations. The plan and agreement provided that petitioner, a new corporation, would result from the merger and consolidation of the old companies.

Rentals on long-term leases, accrued but unpaid, were recorded on the books of account of Philadelphia Rapid Transit Co. in the amounts of $28,692,245.94 as of December 31, 1938, and $35,463,063.74 as of December 31, 1939.

From October 1934 to February 24, 1939, the "Lessor Companies" had received no payments in respect of those leases except three payments aggregating $2,300,000 paid by order of the United States District Court after October 1934 and prior to 1937, $2,000,000 paid pursuant to the order of the United States Circuit Court of Appeals for the Third Circuit on January 3, 1937, and $1,000,000 paid pursuant to order of the United States District Court entered June 6, 1938. All such payments were "ad interim allowances," without prejudice to any question pending in the reorganization proceedings.

On February 24, 1939, Union Traction Co. of Philadelphia, on behalf of itself and other lessor companies, filed a petition for a payment of $3,000,000. This was opposed by the Pennsylvania Public Utility Commission on the ground that such payment would dangerously deplete the working capital of the reorganized company and that the holders of stock and stock trust certificates of the lessor companies under the plan were to receive $2,204,000 in cash.

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On June 1, 1939, said petition of Union Traction Co. was heard by the court and, it appearing that the Pennsylvania Public Utility Commission had given consideration to the amount of cash which after reorganization would be available for rehabilitation and modernization of the system and that the city of Philadelphia had given consent to the action necessary on its part if and when the plan should be approved, the court ordered that an ad interim allowance of $700,000 be made to the Union Traction Co. and stated that such allowance was without prejudice to any question then pending.

Philadelphia Rapid Transit Co. filed a motion (verified on November 13, 1939) for confirmation of the plan, representing that, with the single exception of one class of creditors, all parties in interest including the Pennsylvania Public Utility Commission and the city of Philadelphia, had accepted the plan and that an overwhelming majority of the affected stockholders and creditors, representing in each class a majority in excess of the required statutory majority, had accepted the plan. The "Debtor" submitted drafts, for approval prior to execution, of substantially all documents necessary to consummate the plan, the consolidation of the several corporations, and the transfer of property.

On November 14, 1939, "Drexel & Co., Agent" for each of the corporations which were parties to the plan, filed an "Affidavit re Acceptances of Plan" showing the percentage of acceptances of the plan as of the close of business November 13, 1939, by holders

of affected issues of stock, stock trust certificates, and bonds.

On November 14, 1939, the motion of the "Debtor" for confirmation of the plan was heard. The court found, among other facts, that the plan had been submitted to and approved by the Pennsylvania Public Utility Commission, had been accepted by the city of Philadelphia and by all necessary parties except one class of creditors, for the protection of whose rights provision was made, and that "12. The compromise set forth in the Plan is approved as reasonable, fair and equitable."

The court ordered that:

> 8. The new company, upon confirmation of the Plan, will be authorized to take all action necessary to carry out the Plan and all authorizations, approvals or consents required by law have been obtained.

and that:

> 13. The Plan provides that the new company shall assume liability for the payment of, and will pay in full in cash, all taxes legally due or which may become due to the United States of America, the Commonwealth of Pennsylvania, the City of Philadelphia, and/or any other taxing authority by the debtor, the additional debtors, the trustees thereof, other merging companies and/or wholly-owned subsidiaries whether or not proofs of claim therefor have been filed in this reorganization proceeding (unless such taxes are fully paid and satisfied prior to the confirmation of the Plan) and such taxes shall be assessed against, collected from, and

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paid by transportation company[2] in the same manner subject to the same provisions of law as would be applicable to the debtor, the additional debtors, other merging companies and wholly-owned subsidiaries had this reorganization proceeding not intervened.

and that "15. The Plan is hereby confirmed and approved."

On the same day, November 14, 1939, the court entered an order approving the documents and the terms and procedure for carrying out the order confirming the plan, providing, among other matters, that "3. The transfer books for all securities of all companies parties to the Plan shall be closed as of 3:00 P. M. on the date of this order," and making provision for the adjustment of the interest on the "First and Refunding Bonds of the New Company" and on the "Consolidated Mortgage Bonds of the New Company" in those instances where the holders of bonds which were to be surrendered in exchange for the bonds of the new company had received payments of interest applicable to the year 1939 on their old bonds.

In accordance with the plan and as a result of the "Agreement of Consolidation and Merger," petitioner came into existence as a corporation on January 1, 1940, immediately after midnight, December 31, 1939.

On January 29, 1940, petitioner, pursuant to said plan, executed and delivered its 3 per cent–6 per cent consolidated mortgage bonds in the amount of $32,529,943.54, dated January 1, 1939, and bearing in-

[2] "Transportation company" refers to petitioner.

terest from January 1, 1939,[3] to the Fidelity-Philadelphia Trust Co., then and now trustee for the bondholders, for authentication. The trustee forthwith authenticated the bonds and delivered them to Drexel & Co., depository, for delivery.

Said bonds were secured by a mortgage upon all of the properties of the petitioner, subject only to the prior encumbrances listed in the plan. The trust indenture evidencing the mortgage was executed and delivered by the petitioner on January 4, 1940, and recorded in Philadelphia County, Pennsylvania, on January 9, 1940, in Delaware County, Pennsylvania, on January 10, 1940, in Bucks County, Pennsylvania, on January 11, 1940, and in Montgomery County, Pennsylvania, on January 11, 1940.

On January 29, 1940, petitioner delivered its check in the amount of $977,112 to the trustee for bondholders of the 3 per cent-6 per cent consolidated mortgage bonds, with direction to the trustees to pay to the bondholders an amount equivalent to 3 per cent of the face amount of the respective bonds upon surrender for redemption of coupons numbered 1 and 2 affixed to the bonds, which coupons were designated in the trust indenture as "Fixed Interest Coupons." This transaction was recorded on the books of petitioner by a debit of $977,112 against two items of liability, $966,952.30 and $500, appearing on journal entry No. 1, hereinafter mentioned. Subsequently, the item of

[3] Except that in the case of the $596,400 principal amount of said bonds, heretofore mentioned, "Fixed Interest Coupon No. 1" was removed.

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$977,112 was decreased by proper refunds and credits to $967,452.30. ($966,952.30 plus $500.)

In the operation of an electric railway system petitioner is subject to regulations issued by the Pennsylvania Public Utility Commission and is required to keep its accounts in accordance therewith. Pursuant to such regulations, petitioner prepared its journal entry No. 1, "to Open the Books of Philadelphia Transportation Company on January 1, 1940." This was prepared in the late spring of 1940 as of January 1, 1940.

On journal entry No. 1 "To Open the Books of Philadelphia Transportation on January 1, 1940," under "Liabilities," the following entries were made:

Current liabilities		
Matured Interest Dividends and Rents Unpaid.	$996, 702. 47	
Phila. Rapid Transit Co. Dividends Payable.	1, 257. 50	Unpresented checks at 1/1/40 issued by merged companies.
Lessor Companies Dividends Payable.	2, 466. 87	
Payment of Rent for Use and Occupancy due Lessor Co.'s Stockholders.	3, 353. 74	
Drexel & Co. Agent—Exchange of Doylestown & Willow Grove St. Railway Co. 1st Mtge. Bonds.	500. 00	Payments due under plan of reorganization and/or order of U. S. District Court.
Drexel & Bo. Agent—Exchange of Lessor Companies Bonds for Phila. Transp. Co. 1st & Refunding 4% Bonds.	22, 172. 06	
Fidelity-Phila. Tr. Co. Trustee-Fixed Interest for year 1939 on Phila. Transp. Co. Consolidated Mtge. Bonds "Series A."	966, 952. 30	
Accrued Interest, Dividends & Rents Payable.	1, 629, 979. 39	
Accrued Interest on Funded Debt.	311, 640. 91	Interest accrued but not due at 1/1/40 on all outstanding funded debts of system.
Accrued Interest on Unfunded Debt.	1, 073. 34	Transferred from books of Phila. Rapid Transit Company.
Accrued Rents—City of Phila. Lines.	474, 579. 37	
Accrued Rent—Delaware River Bridge Line.	11, 535. 05	
Accrued Miscellaneous Debits...	925. 54	Accrued balance at 1/1/40 of an amount due for fees for registration of stock, trusteeship of bonds, etc. on issues of securities outstanding after reorganization.
Income Interest on Phila. Transportation Co. Consolidated 3%–6% Bonds.	820, 225. 18	Income interest accrued on Consolidated 3%–6% Bonds for year 1939.

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All of the said items are reflected in petitioner's opening balance sheet as of January 1, 1940.

The liability appearing in the journal entry as "Drexel & Co., Agent—Exchange of Doylestown & Willow Grove St. Railway Co. 1st Mtge. Bonds $500.00" was paid on January 29, 1940, pursuant to court order in the adjustment in respect of 1939 made upon the exchange of petitioner's 3 per cent–6 per cent consolidated mortgage bonds for bonds of "Lessor Companies."

The liability appearing in the journal entry as "Drexel & Co. Agent—Exchange of Lessor Companies Bonds for Phila. Transp. Co. 1st & Refunding 4% Bonds $22,172.06" was entered pursuant to court order in the adjustment in respect of 1939 made upon the exchange of petitioner's first and refunding mortgage 4 per cent bonds for bonds of the "Lessor Companies." This item was not claimed as a deduction from gross income on petitoner's 1940 return.

The liability appearing in the journal entry as "Fidelity-Phila. Tr. Co. Trustee-Fixed Interest for year 1939 on Phila. Transp. Co. Consolidated Mtge. Bonds Series 'A' $996,952.30" was paid as part of the item $977,112 paid by petitioner on January 29, 1940. It was computed as follows:

3% (used to redeem "Fixed Interest Coupons No. 1 and No. 2") on $31,933,543.54 face value of 3%–6% Consolidated Mortgage Bonds issued to stockholders and stock trust certificate holders of 21 "Lessor Companies"	$958,006.30
1.5% (used to redeem "Fixed Interest Coupon No. 2") on $596,400.00 face value of the same bonds issued to holders of "Lessor Companies" bonds on which latter bonds part interest for 1939 had been paid	8,946.00
	966,952.30

The item appearing in the journal entry as "Income Interest on Phila. Transportation Co. Consolidated 3 per cent-6 per cent Bonds $820,225.18" constituted the variable payment on said bonds required to be made on July 1, 1940. It was computed at the rate of 2.52 per cent on $32,529,943.54 face amount of outstanding bonds in accordance with a report made to petitioner by Lybrand, Ross Brothers & Montgomery, certified public accountants, dated April 29, 1940.

In said report, Lybrand, Ross Brothers & Montgomery stated that:

> * * * the holders of your company's Consolidated Mortgage 3%-6% Series A bonds, due January 1, 2039, are to receive income interest not to exceed three per cent based on the net income for the calendar year 1939, under [the hypothesis that] the plan of reorganization being [became] effective as of January 1, 1939. We have stated the income account for the calendar year 1939 after giving effect to said plan. [Words in brackets supplied.]

Rentals payable by the Philadelphia Rapid Transit Co. to the "Lessor Companies" for 1939 in the amount of $7,470,817.80 and an interim payment of $700,000 paid to certain "Lessor Companies" in 1939 in connection with the reorganization proceedings and pursuant to an order of the Federal District Court having jurisdiction thereof, are not reflected in said report.

On June 28, 1940, petitioner delivered its check in the amount of $819,754.48 to the trustee for bondholders of the 3 percent-6 percent consolidated mort-

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gage bonds, with direction to the trustee to pay to the bondholders an amount equivalent to 2.52 per cent of the fact amount of their respective bonds upon surrender for redemption of coupon No. 1 affixed to the bonds, which coupon was designated in the trust indenture as "Income Interest Coupon." This transaction was recorded on the books of petitioner by a debit of $819,754.58 against the liability of $820,225.18 shown on journal entry No. 1. Said sum was paid to the bondholders on July 1, 1940.

In accordance with regulations of the Public Utility Commission of the Commonwealth of Pennsylvania, the payments of $966,952.30 and $500 and $819,754.58 were not charged as an expense in petitioner's accounts for 1940.

Petitioner accrued on its books in 1940 the fixed and income interest payments due with respect to the 3 percent-6 percent consolidated mortgage bonds and payable as follows:

Fixed interest (coupon 3)	July 1, 1940
Fixed interest (coupon 4)	Jan. 1, 1941
Income interest (conpon 2)	July 1, 1941

It deducted these amounts on its tax return for the year 1940 as interest and respondent has allowed the deductions. These deductions are not in issue in this proceeding.

On its corporation income and declared value excess profits tax return for 1940 (Schedule 1–A "Reconciliation of Net Income Year Ending December 31, 1940") petitioner, among other items, subtracted the sum of $1,787,206.88 designated "Payment on Philadelphia Transportation Co. 3%-6% Consolidated

Mortgage Bonds Schedule 12" from "Income per books" to arrive at "Net Income [loss] per Tax Return."

On its Federal income tax return for the calendar year 1940 petitioner claimed as a deduction $1,787,206.88 ($967,452.30 paid in January 1940, plus $819,754.58 paid in July 1940) as interest paid in computing its 1940 taxable income [loss].

Petitioner's consolidated income and declared value excess profits tax return for the calendar year 1940 was filed on July 22, 1941, pursuant to an extension to August 15, 1941, of time for filing duly granted by the respondent on June 4, 1941. No waivers or extensions of the period for assessment were ever filed.

In determining petitioner's net operating loss deduction for 1942, respondent disallowed the item of $1,787,206.88 claimed as a deduction on the return in computing the net operating loss for 1940 to be carried over to 1942. Except for minor items in respect of which the parties are now in agreement, that disallowance is the cause of the deficiency.

By letter dated September 23, 1940, petitioner asked respondent for a specific ruling. A letter to petitioner dated October 9, 1940, signed "Timothy C. Mooney, Deputy Commissioner by L. K. Sunderlin, Chief of Section," stated:

> Mr. Renner has requested a specific ruling with regard to the treatment, for the purposes of the Federal income tax, of the amounts paid by your company as interest on its Consolidated Mortgage Bonds, the filing of ownership cer-

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tificates on form 1012 with respect to such interest payments, and the withholding of tax at the source with regard to the interest payments made to nonresident alien stockholders.

and ruled:

> * * * The distribution under consideration in the instant case is held to represent a payment of interest on an outstanding obligation. Accordingly, as the payments made in January 1940 represent payments of interest, ownership certificates are required with respect to such payments. Furthermore, tax at the prescribed rate must be deducted and withheld from all payments of interest made to nonresident alien bondholders. (Section 143 (b) of the Internal Revenue Code and section 143 (b) of the Internal Revenue Code, as amended.)

On its return for 1940 petitioner reported a "Normal net income" [loss] of $3,077,666.75, computed as follows:

Reconciliation of Net Income, Year Ending December 31, 1940

Income per books		$185,624.25
Additions:		
Net short term capital gain Schedule # 2	$70.22	
Federal Income Tax Schedule #3	47,696.09	47,766.31
		233,390.56
Deductions:		
Payments on Phila. Transportation Co. 3%–6% Consolidated Mortgage Bonds Schedule 12	1,787,206.88	
Depreciation—Excess of schedule over books Schedule #15	961,482.54	
Other deductions not here material	549,744.88	
	3,298,434.30	
85% of Dividends Received, Schedule #7	12,623.01	3,311,057.31
	(Loss)	3,077,666.75

The internal revenue agent in charge at Philadelphia, Pennsylvania, wrote petitioner under date of January 19, 1943, as follows:

> In re: Income Tax Return
> Year(s) covered: 1940
>
> Upon examination of your income tax return(s) for the year(s) indicated above, the conclusion has been reached that it (they) should be accepted as filed.
>
> I am sure you will appreciate that should subsequent information be received which would materially change the amount reported, it will be necessary under existing laws to redetermine your tax liability.

OPINION

HARLAN, *Judge:* The respondent contends that the payments made by petitioner in the redemption of the 1939 coupons were not payments of interest; that the obligation to redeem the 1939 coupons did not accrue in 1940; that it was imposed in 1939 and became a fixed liability on November 14, 1939; that the 1939 coupons were to counterbalance the difference between 1939 rentals and the $700,000 *ad interim* payment; that the amount of $1,787,206.88 paid to redeem the 1939 coupons was computed on 1939 income; that it is treated on petitioner's books exactly in accordance with respondent's determination; that this obligation became fixed in 1939; that petitioner may not in 1940 accrue "interest" on the same obligation for the years 1939 and 1940; and that the accrual of the alleged 1939 interest on the accrual of the actual

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1940 interest as deductions from gross income of 1940 distorts petitioner's net operating loss for that year.

The petitioner contends that the amounts it paid in redemption of the 1939 coupons on its 3 percent-6 percent consolidated mortgage bonds constituted interest on indebtedness which accrued in 1940 and hence was deductible from gross income for that year. In the alternative it contends that the deductions claimed on its 1940 income tax return were allowed by the respondent within the meaning of the Internal Revenue Code, and respondent, therefore, erred in disregarding them in computing its income-tax liability for 1942.

Section 23 (b) of the Internal Revenue Code permits a taxpayer to deduct all interest paid or accrued within the taxable year on indebtedness.

This Court has held in a number of cases, relied upon and cited by petitioner, that interest accrued or paid under circumstances substantially the same as those here involved is deductible. *Columbia River Paper Mills,* 43 B. T. A. 104; affd., 126 Fed. (2d) 1009; *Oregon Pulp & Paper Co.,* 47 B. T. A. 772 (petition for review dismissed, C. C. A., 9th Cir., Nov. 2, 1943); *Ernst Kern Co.,* 1 T. C. 249; *Pressed Steel Car Co.* v. *Commissioner,* 152 Fed. (2d) 280, affirming per curiam, Tax Court memorandum opinion, Docket No. 107623, August 16, 1944. The Circuit Court of Appeals for the Seventh Circuit reached a contrary conclusion on similar facts in *Commissioner* v. *Drovers Journal Publishing Co.,* 135 Fed. (2d) 276. The latter case is relied upon by the respondent.

The above-cited cases, excluding the *Drovers* case, which we respectfully decline to follow, require that our decision on the issue presented for our consideration be in favor of petitioner. Having reached this conclusion, no useful purpose would be served by any detailed discussion of the respondent's contentions and argument. Suffice to say that we do not have before us the question of the tax treatment to be accorded purchase money applied to an indebtedness existing prior to the acquisition of property, or an instance where property was acquired subject to the obligation of a third party. Cases such as *Pratt-Mallory Co.* v. *United States* (Ct. Cls.), 12 Fed Supp. 1020, 1023; *Rodney, Inc.,* v. *Commissioner,* 145 Fed. (2d) 692, affirming 2 T. C. 1020; *Koppers Co.,* 3 T. C. 62; affd., 151 Fed. (2d) 267; *Magruder* v. *Supplee,* 316 U. S. 394; *Automatic Sprinkler Co. of America,* 27 B. T. A. 160, cited by respondent, do not, therefore, have any application here. The plan of reorganization does not contain any provision imposing upon petitioner, as the new company, a liability to discharge the obligation of any other party to the reorganization to pay rentals or interest. When petitioner made the payments in redemption of the 1939 coupons it was paying its own obligation—not that of another party. The 3 per cent–6 per cent consolidated mortgage bonds constituted an indebtedness of petitioner. These bonds and the coupons in redemption of which the payments in controversy were made, all required the payment of the questioned sums as interest. The respondent himself recognized that these payments constituted inter-

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est when, on October 9, 1940, in advising petitioner that it was required to withhold income tax on payments made to nonresident alien bondholders, he said: "The distribution under consideration in the instant case is held to represent a payment of interest on an outstanding obligation." Inasmuch as petitioner did not come into existence until 1940, did not issue its bonds until 1940, did not exchange them with the depositing security holders in the reorganization proceedings until 1940, and did not actually undertake any liability until all these things had taken place, it was impossible for the interest to accrue prior to 1940. Inherent in the accrual of an obligation is the existence of an obligor, and petitioner's obligation accrued in 1940 when it came into existence and was legally capable of contracting obligations. We hold that the petitioner properly accrued and deducted in its income tax return for 1940, interest in the amount of $1,787,-206.88 which it paid in that year.

Having reached this conclusion, we deem it unnecessary to discuss or decide the petitioner's alternative contention.

Reviewed by the Court.

Decision will be entered under Rule 50.

THE TAX COURT OF THE UNITED STATES

Washington 25, D. C.

Docket No. 9893

PHILADELPHIA TRANSPORTATION COMPANY,
PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE,
RESPONDENT

DECISION

Pursuant to the Court Findings of Facts and Opinion, promulgated November 28, 1947, the parties herein having filed an agreed computation of tax on February 17, 1948, it is

Ordered and decided: That there is an overpayment in income tax for the calendar year 1942, of $699,063.69, which amount was paid after the mailing of the notice of deficiency.

Entered Feb. 19, 1948.

(Signed) BYRON B. HARLAN,
Judge.

U. S. GOVERNMENT PRINTING OFFICE: 1948

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EXHIBIT 3-C: PLAN OF REORGANIZATION.

Second Revised

PLAN OF REORGANIZATION

of

PHILADELPHIA RAPID TRANSIT COMPANY SYSTEM

Dated December 1, 1937
Amended June 1, 1938 and November 15, 1938

THE NATURE OF THE PLAN.

Under the Plan, Philadelphia Rapid Transit Company (hereinafter called "P.R.T.") and present Lessor Companies will merge to form a new company, PHILADELPHIA TRANSPORTATION COMPANY (hereinafter called "Transportation Company") which will be a single owning and operating company. The public holders of stock and stock trust certificates of Lessor Companies will receive in exchange for their present securities, approximately $31,974,000 face amount of 3%-6% Consolidated Mortgage Bonds and approximately $12,301,000 par value of Participating Preferred Stock (of a par value of $20 per share) of Transportation Company and approximately $2,204,000 in cash, as hereinafter set forth. The total fixed annual interest (3%) on the said new bonds will be approximately $6,141,000 less, and the total maximum interest payable if earned (6%) on the said new bonds will be approximately $5,182,000 less, than the annual rentals formerly paid to the holders of such securities of Lessor Companies under the old leases. The accumulated dividends on P.R.T. Preferred Stock will be waived and the

holders of such stock will receive, in exchange for each share of P.R.T. Preferred Stock, one half share of Participating Preferred Stock of Transportation Company and one half share of Common Stock of Transportation Company and $1 in cash. The holders of P.R.T. Common Stock will receive one share of Common Stock of Transportation Company in exchange for each share of P.R.T. Common Stock. Certain funded debt of P.R.T. and of Lessor Companies will be refunded with new bonds or obligations of Transportation Company and the balance of the present funded debt of said companies will remain outstanding and become, by virtue of the merger, the obligations of Transportation Company, which will assume all obligations of merging companies. Certain mortgages and ground rents on property of merging companies or their wholly-owned subsidiaries will remain outstanding.

THE PLAN.

SECTION 1. *The Corporations Parties to the Plan*

The Corporations Parties to the Plan will be:

Philadelphia Rapid Transit Company and twenty-seven street railway and traction companies herein referred to collectively as "Lessor Companies" and classified, for purposes of the Plan, in three classes, as follows:

Class A Lessor Companies, viz:

street railway companies whose systems are leased to intermediate traction companies listed below as "Class B Lessor Companies", such Class A Lessor Companies being as follows:

Catherine and Bainbridge Streets Railway Company of the City of Philadelphia, The,
Citizens Passenger Railway Company of Philadelphia,

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Continental Passenger Railway Company of Philadelphia,
Empire Passenger Railway Company of Philadelphia,
Fairmount Park and Haddington Passenger Railway Company, The,
Frankford and Southwark Philadelphia City Passenger Railroad Company,
Germantown Passenger Railway Company,
Green and Coates Street Philadelphia Passenger Railway Company,
Peoples Passenger Railway Company,
Philadelphia City Passenger Railway Company,
Philadelphia and Darby Railway Company, The,
Philadelphia and Gray's Ferry Passenger Railway Company,
Ridge Avenue Passenger Railway Company,
Second and Third Streets Passenger Railway Company of Philadelphia,
Seventeenth and Nineteenth Streets Passenger Railway Company of Philadelphia,
Thirteenth and Fifteenth Streets Passenger Railway Company of the City of Philadelphia,
Union Passenger Railway Company of Philadelphia,
West Philadelphia Passenger Railway Company.

Class B Lessor Companies, viz:

intermediate traction and street railway companies whose systems are leased to Union Traction Company of Philadelphia listed below under "Class C Lessor Companies", such Class B Lessor Companies being as follows:

Philadelphia Traction Company,
Electric Traction Company of Philadelphia, The,
Peoples Traction Company,
Hestonville, Mantua and Fairmount Passenger Railroad Company.

Class C Lessor Companies, viz:

traction and street railway companies, other than wholly owned subsidiaries of P.R.T., whose systems are leased direct to P.R.T., such Class C Lessor Companies being as follows:

Union Traction Company of Philadelphia,
Darby, Media and Chester Street Railway Company,
Darby & Yeadon Street Railway Company,
Doylestown and Willow Grove Railway Company,
Philadelphia and Willow Grove Street Railway Company.

SECTION 2. *Formation of Philadelphia Transportation Company.*

By a Merger Agreement in a form to be approved by or on behalf of all corporations parties to the Plan, P.R.T., all Lessor Companies and street railway companies whose stock is wholly owned by Lessor Companies and/or P.R.T. as listed in Schedule "A" hereto attached and made a part hereof, will merge into a single company with the corporate title "Philadelphia Transportation Company". By virtue of this merger Transportation Company will own, either directly or through stock ownership, all franchises and property owned by P.R.T. or leased to P.R.T. by merging companies. The ownership will be direct except in the case of certain subsidiaries of merging companies listed in Schedule "B" attached which will remain in existence as subsidiaries of Transportation Company. Property not owned by or leased to P.R.T. and property (other than securities of any system company) representing the sale proceeds of property formerly covered by the old leases, now held in special funds subject to the leases, is not included in the merger.

As a part of the Plan, and either prior to or subsequent to the aforesaid merger: (1) P.R.T. or its successor, Transportation Company, will acquire all the

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corporate powers, franchises, property, rights and credits of Philadelphia Rural Transit Company, under and pursuant to the Act of June 26, 1931, P. L. 1402; (2) Darby, Media and Chester Street Railway Company or its successor, Transportation Company, will acquire all the corporate powers, franchises, property, rights and credits of D M & C Bus Company, under and pursuant to the Act of June 26, 1931, P. L. 1402; and (3) P.R.T. or its successor, Transportation Company, will acquire all the corporate powers, franchises, property, rights and credits of Pennsylvania Rapid Transit Company, under and pursuant to the Act of July 2, 1937, P. L. 2824. The corporate powers, franchises, property, rights and credits so acquired will, following such acquisition and the aforesaid merger, be owned by Transportation Company.

SECTION 3. *Capitalization of Transportation Company.*

The authorized capitalization of Transportation Company will be as follows:

(a) *First and Refunding Mortgage Bonds:*

These bonds will be secured by a Mortgage and Deed of Trust creating a direct lien upon all surface railway and motor bus franchises and lines owned by Transportation Company and all real estate used in connection with such surface lines and certain additional real estate, (the lien on which said real estate owned by wholly-owned subsidiaries will be created by adherence mortgage), subject only to such existing prior lien bonds, mortgages and ground rents as are not to be presently refunded, as shown on Schedule "C". The First and Refunding Mortgage Bonds will be further secured by the pledge of the equity in the stock of Market Street Elevated Passenger Railway Company. Bonds secured by this First and Refunding Mortgage will be issuable for the following purposes only:

(i) For refunding purposes as follows:

To refund the bonds listed below in Section 4 (e);

To refund First and Refunding Mortgage Bonds as the same may from time to time mature;

To refund certain bonds, mortgages and ground rents of, or on property owned by, companies merging to form Transportation Company and companies which will be wholly-owned subsidiaries of Transportation Company, as shown in Schedule "C";

To refund any other funded debt, mortgages or ground rents which may at any time be a direct prior lien on property subject or made subject to the lien of the First and Refunding Mortgage; subject, however, as a condition precedent to such refunding, to a certificate of one or more engineers or other representatives, selected by the corporate Trustees of the First and Refunding and Consolidated Mortgage Bonds, that such refunding is reasonably necessary and proper for the preservation and efficient operation of the property or business of Transportation Company and/or its wholly-owned subsidiaries.

(ii) To provide new capital up to not more than 75% of the cost or value of additions, betterments or extensions to the property of Transportation Company and/or its wholly-owned subsidiaries. The mortgage will require, as a condition precedent to the issue of bonds for this purpose, a certificate of one or more engineers or other representatives, selected by the corporate Trustees of the First and Refunding and Consolidated Mortgage Bonds, as to the cost and value of such additions, betterments or extensions and as to the fact that they are reasonably necessary and proper for the efficient operation and/or extension of the property or business of Transportation Company and/or its wholly-owned subsidiaries.

The Mortgage and Deed of Trust securing these First and Refunding Mortgage Bonds will provide for

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the issue of bonds from time to time for the purposes above set forth in different series with different maturities, different rates of interest, different call provisions, and other different provisions; and will provide for the release of the lien thereof on any property which may become no longer used or useful in the business of Transportation Company, upon the payment of the salvage proceeds thereof, if any, to the Trustee either for the sinking fund or for use for additions, betterments and extensions to property subject or made subject to the lien thereof and if a new transportation facility is substituted for such property so abandoned Transportation Company's property interest in the same shall be made subject to the lien thereof either directly or through stock ownership.

The Mortgage and Deed of Trust will contain sinking fund provisions requiring the payment to the Trustee annually of an amount equal to One per cent. (1%) of the maximum face amount of First and Refunding Mortgage Bonds which shall at any one time have been outstanding in the hands of the public. Bonds held in the treasury of Transportation Company, whether or not pledged, and bonds held in the sinking fund shall not be deemed to be outstanding for the purpose of computing sinking fund payments. Bonds purchased for the sinking fund shall be kept alive and the interest thereon added to the sinking fund payments. If at any time all outstanding First and Refunding Mortgage Bonds shall be paid and cancelled, the bonds held in the sinking fund shall be cancelled. If at any subsequent time there are such bonds issued and outstanding, the amount thereof shall be taken, as aforesaid, as the amount on the basis of which payments into the sinking fund shall be calculated. This sinking fund will be applicable to the purchase of First and Refunding Mortgage Bonds and/or prior lien bonds, mortgages and ground rents shown on Schedule "C", or which may be refundable by First and Refunding Mortgage Bonds as aforesaid.

The Mortgage and Deed of Trust will be in a form to be approved by or on behalf of all corporations parties to the Plan.

All of the First and Refunding Mortgage Bonds to be presently issued and distributed as set forth in Section 4 (e) of this Plan will be of a single series and will be dated January 1, 1939 and mature on January 1, 1969, will bear interest at the rate of 4% per annum, with a provision requiring Transportation Company to pay interest without deduction for any Pennsylvania Personal Property Taxes or Corporate Loans Taxes not in excess of five mills per annum in the aggregate and will be callable by Transportation Company, or by the Trustee of the sinking fund, at any time, in whole or in part, at face amount and accrued interest.

(b) *Consolidated Mortgage Bonds:*

These bonds will be secured by a Mortgage and Deed of Trust junior to the Mortgage and Deed of Trust securing the First and Refunding Mortgage Bonds above described and covering the same franchises and properties. Bonds secured by this Consolidated Mortgage and Deed of Trust will be issuable for the following purposes only:

(i) In exchange for stock and/or stock trust certificates of Lessor Companies outstanding in the hands of the public and/or pledged to secure outstanding collateral trust bonds, as hereafter in Section 4 of this Plan set forth.

(ii) For refunding the bonds listed below in Section 4 (f) and for refunding Consolidated Mortgage Bonds and also for other refunding and additions, betterments and extensions as hereinbefore set forth in the case of the First and Refunding Bonds under paragraphs (a), (i) and (ii) of this Section and subject to the same restrictions and conditions.

The Mortgage and Deed of Trust securing these Consolidated Mortgage Bonds will provide for the issue of

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bonds from time to time for the purposes set forth above in different series with different maturities, different rates of interest, different sinking fund provisions and different call provisions, and other different provisions; and will provide for the release of the lien thereof on any property which may become no longer used or useful in the business of Transportation Company, upon the payment of the salvage proceeds thereof, if any, to the Trustee either for the sinking fund or for use for additions, betterments and extensions to property subject or made subject to the lien thereof and if a new transportation facility is substituted for such property so abandoned Transportation Company's property interest in the same shall be made subject to the lien thereof either directly or through stock ownership.

The Mortgage and Deed of Trust will contain sinking fund provisions as follows:

When and as the present sinking fund requirements of the outstanding bonds of merging companies and/or of wholly-owned subsidiaries are reduced through retirement or refunding of such bonds, payments equal to the amount of such reductions, but not exceeding in the aggregate $300,000 per year, shall be made annually into a sinking fund in the hands of the Trustee of the Consolidated Mortgage Bonds. Transportation Company will also covenant that in any year in which it shall pay any dividend on its Common Stock it will, before paying such dividend, pay into such sinking fund the additional sum of $200,000. The sinking fund for the Consolidated Mortgage Bonds shall be applied to the purchase, at not exceeding face value, of Consolidated Mortgage Bonds. Bonds purchased for the sinking fund shall be cancelled.

The Mortgage and Deed of Trust will be in a form to be approved by or on behalf of all corporations parties to the Plan.

All of the Consolidated Mortgage Bonds to be presently issued and distributed as set forth in Section 4 (a) and (f) of this Plan will be of a single series and will be dated January 1, 1939 and mature on January 1, 2039.

They will bear a fixed rate of interest at the rate of 3% per annum and in any year in which Transportation Company would have net income otherwise available for dividends, then such income shall be applied toward the payment of additional interest upon the said Bonds; Provided, however, that such payments of additional interest on said Bonds shall be to the nearest ½ of 1% for which such net income is available and shall never for any year exceed 3% in addition to the fixed interest of 3% per annum. Such additional interest shall be non-cumulative and shall be paid only for such years in which the same shall be earned as aforesaid. There will be a provision requiring Transportation Company to pay interest without deduction for any Pennsylvania Personal Property Taxes or Corporate Loans Taxes not in excess of five mills per annum in the aggregate and said bonds will be callable by Transportation Company, or by the Trustee of the sinking fund, at any time, in whole or in part, at face amount and accrued interest.

(c) *Certain Prior Lien Bonds, Mortgages and Ground Rents to Remain Outstanding:*

In addition to the First and Refunding and Consolidated Mortgage Bonds to be issued by Transportation Company as set forth in (a) and (b) above, there will remain outstanding certain now existing prior lien bonds, mortgages and ground rents of, or on property owned by, companies merging to form Transportation Company and companies which will be wholly owned subsidiaries of Transportation Company, as shown in Schedules "E-1," "E-2" and "E-3."

(d) *Participating Preferred Stock:*

A presently authorized issue of approximately 755,100 shares of Participating Preferred Stock, par value $20 per share. This Participating Preferred Stock will have voting rights share for share with the Common Stock and will be non-cumulative, unless earned. It will be entitled

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to receive a prior preferred dividend of $1.00 per share in or for any year before the payment of any dividends on the Common Stock, in or for such year. After the Participating Preferred Stock shall have received a dividend of $1.00 per share in or for any one year it will not then be entitled to receive any further dividend in or for such year unless a dividend of $1.00 per share shall have been paid in or for such year on the Common Stock; after the Common Stock shall have received a dividend of $1.00 per share in or for such year, the Participating Preferred Stock will then be entitled to participate with the Common Stock in all further dividends paid in or for such year as follows: the amount of such further dividend per share of the Participating Preferred Stock shall be one and one-half times the amount of such further dividend per share of the Common Stock. Such Participating Preferred Stock shall be in a form, as to all of its terms, to be approved by or on behalf of all corporations parties to the Plan. Participating Preferred Stock shall be redeemable by Transportation Company at any time, in whole or in part, at the par value thereof.

(e) *Common Stock:*

A presently authorized issue of approximately 720,000 shares of Common Stock of no par value with voting rights share for share with the Participating Preferred Stock.

SECTION 4. *Distribution of Securities of Transportation Company.*

The present distribution of securities of Transportation Company will be as follows:

(a) To holders of stock and/or stock trust certificates of Class A, B and C Lessor Companies, outstanding in the hands of the public, approximately $31,974,000 face amount of 3%-6% Consolidated Mortgage Bonds. The precise amount of such 3%-6% Consolidated Mortgage Bonds to be issued in exchange for the stock and/or stock trust certificates of each Lessor Company is shown in

Schedule "D" attached.* These Bonds will be of the 3%-6% series maturing January 1, 2039 described in Section 3 (b) above.

(b) To holders of stock and/or stock trust certificates of Class A, B and C Lessor Companies, outstanding in the hands of the public, approximately 615,100 shares of Participating Preferred Stock of Transportation Company. The precise amount of such Participating Preferred Stock to be issued in exchange for the stock and/or stock trust certificates of each Lessor Company is shown in Schedule "D" attached.

(c) To holders of the 280,000 outstanding shares of 7% Cumulative Preferred Stock of P.R.T., 140,000 shares of Participating Preferred Stock of Transportation Company and 140,000 shares of Common Stock of Transportation Company.

(d) To holders of the 579,926 outstanding shares of Common Stock of P.R.T., 579,926 shares of Common Stock of Transportation Company.

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*In addition to the Consolidated Mortgage Bonds to be issued in exchange for stock and/or stock trust certificates of Lessor Companies as set forth in Schedule "D", and in addition to the Consolidated Mortgage Bonds to be issued in refunding outstanding bonds of Lessor Companies as set forth in Section 4 (f) below, there will also be issued: (1) to the Trustee of $523,000 face amount of Union Traction Company of Philadelphia 4% Sinking Fund Collateral Trust Mortgage Bonds due July 1, 1952, outstanding, in exchange for the existing collateral security therefor, $2,333,400 face amount of 3%-6% Consolidated Mortgage Bonds of Transportation Company due January 1, 2039 described in Section 3 (b); and (2) to the Trustee of $2,107,000 face amount of Philadelphia Rapid Transit Company 5% Collateral Bonds due February 1, 1957, outstanding, in exchange for the existing collateral security therefor, $9,476,700 face amount of said 3%-6% Consolidated Mortgage Bonds. These said additional Consolidated Mortgage Bonds, which will be in the total face amount of $11,810,100, will be owned by Transportation Company and not outstanding in the hands of the public but held by the Trustees for the aforesaid collateral trust bonds as collateral security therefor; the said two respective amounts of said Consolidated Mortgage Bonds are in such amount that the fixed interest thereon would equal the interest and sinking fund payments required by the indentures under which the aforesaid respective collateral trust bonds were issued. Such Consolidated Mortgage Bonds shall be cancelled upon the retirement of the said respective obligations which they will secure.

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(e) To holders of $1,897,860 face amount of outstanding bonds of Lessor Companies listed below, in exchange therefor, $1,897,860 face amount of the First and Refunding 4% Mortgage Bonds of Transportation Company, due January 1, 1969, described in section 3 (a) above:

	Face Amount Outstanding in Hands of Public
Darby & Yeadon Street Railway Company 4½% First Mortgage Bonds, due December 1, 1934	$200,000
Peoples Passenger Railway Company 4% First Mortgage Bonds, due January 15, 1935	219,000
Philadelphia City Passenger Railway Company 5% Debenture Bonds, due March 1, 1935	100,000
Empire Passenger Railway Company of Philadelphia 6% First Mortgage Bonds, due March 1, 1935	100,000*
Catherine and Bainbridge Streets Railway Company of the City of Philadelphia, The, 6% First Mortgage Bonds, due April 1, 1935	150,000
Frankford and Southwark Philadelphia City Passenger Railroad Company (West End Passenger Railway Company) 4% First Mortgage Bonds, due October 1, 1935	132,100
Hestonville, Mantua and Fairmount Passenger Railroad Company 5½% Consolidated Bonds, due May 1, 1934 and May 1, 1939	896,760
Seventeenth and Nineteenth Streets Passenger Railway Company of Philadelphia 6% First Mortgage Bonds, due July 1, 1939	100,000
TOTAL	$1,897,860*

*$100,000 face amount additional First and Refunding 4% Mortgage Bonds of Transportation Company will be issued to refund an additional $100,000 face amount of Empire Pass. Ry. Co. of Phila. 6% First Mtge. Bonds due March 1, 1935. Said additional First and Refunding Bonds will be owned by Transportation Company and not outstanding in the hands of the public but held by the Trustee of the sinking fund for the Phila. & Willow Grove St. Ry. Co. 4½% Mtge. Bonds due July 1, 1939; they will be cancelled when said obligations they will secure are retired.

(f) To holders of $1,491,000 face amount of the outstanding bonds of Lessor Companies listed below, in exchange therefor, $596,400 face amount of the 3%-6% Consolidated Mortgage Bonds of Transportation Company, due January 1, 2039, described in section 3 (b) above:

	Present Face Amount	*Face Amount of New Bonds to be Issued*
Darby, Media and Chester Street Railway Company 4½% First Mortgage Bonds, due July 1, 1936	$991,000	$396,400
Doylestown and Willow Grove Railway Company First Mortgage 4% Bonds, due June 1, 1960....	500,000	200,000
TOTAL.....	$1,491,000	$596,400

The totals of all classes of capital securities of, and of bonds, mortgages and ground rents on the property of, Transportation Company and/or its wholly-owned subsidiaries to be issued and outstanding in the hands of the public upon the effectuation of the Plan are shown in Schedule "E" attached. The amount thereof will be approximately $85,015,193.42.

SECTION 5. *Distribution of Cash.*

(a) The stock and stock trust certificates of Lessor Companies held by the public will be exchanged for the amounts of cash and securities of Transportation Company set forth in Schedule "D". The cash payments therefor will total approximately $2,204,000.

(b) The 7% Cumulative Preferred Stock of P.R.T. will be exchanged for cash and Participating Preferred Stock and Common Stock of Transportation Company as set forth in Section 6. The cash payments therefor will total $280,000.

(c) All claims incident to or arising out of the ordinary operation of the P.R.T. System whether founded in

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contract or in tort, and including taxes, will, under the Plan, be paid in due course in cash.

(d) Transportation Company shall assume liability for the payment of, and will pay in full in cash, all taxes legally due or which may become due to the United States of America, the Commonwealth of Pennsylvania, the City of Philadelphia and/or any other taxing authority by the Debtor, the Additional Debtors, the Trustees thereof, other merging companies and/or wholly-owned subsidiaries whether or not proofs of claim therefor have been filed in this reorganization proceeding (unless such taxes are fully paid and satisfied prior to the confirmation of this Second Revised Plan of Reorganization) and such taxes shall be assessed against, collected from, and paid by Transportation Company in the same manner and subject to the same provisions of law as would be applicable to the Debtor, the Additional Debtors, other merging companies and wholly-owned subsidiaries had this reorganization proceeding not intervened.

(e) Reasonable compensation for services rendered and reimbursement for the actual and necessary expenses incurred in connection with the reorganization proceedings and the Plan, as may be duly authorized and approved by the Court, shall be paid in cash.

(f) The balance of cash in the P.R.T. treasury will be turned into the treasury of Transportation Company and shall be applicable to its corporate purposes, except that said cash shall not be used for the payment of any dividends on any stock of Transportation Company.

(g) No further payments on account of rent or use and occupancy will be made unless ordered by the Court.

SECTION 6. *Modification of Rights of P.R.T. Stockholders.*

The holders of P.R.T. Preferred Stock will waive their right to receive all unpaid and accumulated divi-

dends and will convert their holdings of P.R.T. Preferred Stock one half into Participating Preferred Stock of Transportation Company and one half into Common Stock of Transportation Company, so that in place of 280,000 shares of P.R.T. Preferred Stock presently outstanding (of a par value of $50 per share) they will receive 140,000 shares of Participating Preferred Stock of Transportation Company of a par value of $20 per share and 140,000 shares of no par Common Stock of Transportation Company; and the holders of P.R.T. Preferred Stock will also receive $1 in cash for each share thereof at the time of said exchange. The P.R.T. Common Stockholders will convert their holdings of P.R.T. Common Stock, share for share, into no par Common Stock of Transportation Company.

SECTION 7. *Compromise of All Claims and Litigation and Classification of Claims of Creditors and Interests of Stockholders.*

This plan is proposed by P.R.T. as one to be accepted by all parties in interest in compromise of all claims of all kinds and of all pending litigation in the reorganization proceedings, either in the District Court or on appeal in the Circuit Court of Appeals. For the purposes of this Plan, therefore, the claims of creditors and the interests of stockholders of all corporations parties to the Plan are allowed and classified as follows,* the holders of each security of a different nature comprising a separate class:

* To comply with the technical requirements of the Federal Bankruptcy Act as amended, not only is stock of corporations parties to the Plan which is outstanding in the hands of the public classified but also stock of such corporations is classified even though it is (1) inter-company owned and held by P.R.T. as owner or lessee or (2) is pledged as collateral security for stock trust certificates which are also classified. There is no duplication in making the latter classifications for the holders of the stock trust certificates must be classified as creditors whereas the stock (which is held by the trustees of the issues of the stock trust certificates, and not by the stock trust certificate holders themselves) must also be classified to comply with the technical requirements of the Federal Bankruptcy Act as mentioned above; the holders of stock trust certificates will have no duplicate voting rights.

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(a) The following separate classes of holders of outstanding stock whose rights are modified or altered by the Plan:

	Total Shares Outstanding
(1) Philadelphia Rapid Transit Company—Preferred Stock	280,000
(2) Philadelphia Rapid Transit Company—Common Stock	579,926
(3) Catherine and Bainbridge Streets Railway Company of the City of Philadelphia, The	8,000
(4) Citizens Passenger Railway Company of Philadelphia	10,000
(5) Continental Passenger Railway Company of Philadelphia	20,000
(6) Empire Passenger Railway Company of Philadelphia	12,000
(7) Fairmount Park and Haddington Passenger Railway Company, The	6,000
(8) Frankford and Southwark Philadelphia City Passenger Railroad Company	37,500
(9) Germantown Passenger Railway Company	30,000
(10) Green and Coates Streets Philadelphia Passenger Railway Company	10,000
(11) Peoples Passenger Railway Company—Common Stock	60,000
(12) Peoples Passenger Railway Company—Preferred Stock	23,000
(13) Philadelphia City Passenger Railway Company	20,000
(14) Philadelphia and Darby Railway Company, The	4,000
(15) Philadelphia and Grays Ferry Passenger Railway Company	12,388
(16) Ridge Avenue Passenger Railway Company	15,000

	Total Shares Outstanding
(17) Second and Third Streets Passenger Railway Company of Philadelphia	21,204
(18) Seventeenth and Nineteenth Streets Passenger Railway Company of Philadelphia	10,000
(19) Thirteenth and Fifteenth Streets Passenger Railway Company of the City of Philadelphia	20,000
(20) Union Passenger Railway Company of Philadelphia	30,000
(21) West Philadelphia Passenger Railway Company	15,000
(22) Electric Traction Company of Philadelphia, The	175,000
(23) Peoples Traction Company	200,000
(24) Hestonville, Mantua and Fairmount Passenger Railroad Company — Common Stock	39,322
(25) Hestonville, Mantua and Fairmount Passenger Railroad Company — Preferred Stock	10,678
(26) Philadelphia Traction Company	400,000
(27) Union Traction Company of Philadelphia	600,000
(28) Darby, Media and Chester Street Railway Company	17,000
(29) Darby and Yeadon Street Railway Company	100
(30) Doylestown and Willow Grove Railway Company	10,000
(31) Philadelphia and Willow Grove Street Railway Company	2,016

The Plan is conditioned upon its acceptance by a majority in amount of each such class of outstanding stockholders.

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(b) The following separate classes of holders of outstanding bonds and stock trust certificates whose rights are modified or altered by the Plan:

	Face Amount Outstanding in Hands of Public
(32) Catherine and Bainbridge Streets Railway Company of the City of Philadelphia, The, First Mortgage 6% Bonds, due April 1, 1935	$150,000
(33) Darby, Media and Chester Street Railway Company First Mortgage 4½% Bonds, due July 1, 1936	991,000
(34) Darby and Yeadon Street Railway Company First Mortgage 4½% Bonds, due December 1, 1934	200,000
(35) Doylestown and Willow Grove Railway Company First Mortgage 4% Bonds, due June 1, 1960	500,000
(36) Empire Passenger Railway Company of Philadelphia 6% First Mortgage Bond, due March 1, 1935	100,000¶
(37) Frankford and Southwark Philadelphia City Passenger Railroad Company, (West End Passenger Railway Company) First Mortgage 4% Bonds, due October 1, 1935	132,100
(38) Hestonville, Mantua and Fairmount Passenger Railroad Company 5½% Consolidated Bonds, due May 1, 1934 and May 1, 1939	896,760
(39) Peoples Passenger Railway Company First Mortgage 4% Bonds, due January 15, 1935	219,000

¶ $100,000 face amount of additional Empire Pass. Ry. Co. of Phila. 6% 1st Mtge. Bonds, due March 1, 1935, held by the Trustee of the sinking fund for the Phila. & Willow Grove St. Ry. Co. 4½% Mtge. Bonds, due July 1, 1939, will be refunded with $100,000 face amount First and Refunding 4% Mortgage Bonds of Transportation Company which will be owned by Transportation Company and not outstanding in the hands of the public held by said sinking fund Trustee, and will be cancelled upon the retirement of said obligations which they will secure.

	Face Amount Outstanding in Hands of Public
(40) Philadelphia City Passenger Railway Company 5% Debenture Coupon Bonds, due March 1, 1935.....	$100,000
(41) Philadelphia Rapid Transit Company 5% Collateral Bonds, due February 1, 1957	2,107,000*†
(42) Philadelphia and Willow Grove Street Railway Company 4½% Mortgage Bonds, due July 1, 1939.....	363,300‡
(43) Seventeenth and Nineteenth Streets Passenger Railway Company of Philadelphia First Mortgage 6% Bonds, due July 1, 1939.....	100,000
(44) Union Traction Company of Philadelphia 4% Fifty Year Sinking Fund Collateral Trust Mortgage Bonds, due July 1, 1952.....	523,000§

*Estimated amount giving effect to estimated sinking fund retirements to January 1, 1939.

†These bonds are to remain outstanding, the collateral therefor to be exchanged for $9,476,700 face amount of 3%-6% Consolidated Mortgage Bonds of Transportation Company due January 1, 2039 described in Section 3 (b) above which will be owned by Transportation Company and not outstanding in the hands of the public but held by the Trustee for the P.R.T. Co. 5% Collateral Bonds, due February 1, 1957 and will be cancelled upon the retirement of said obligations which they will secure.

‡These bonds are to remain outstanding, some of the securities in the sinking fund therefor, viz., $100,000 face amount of Empire Pass. Ry. Co. of Phila., 6% 1st Mtge. Bonds, due Mar. 1, 1935 to be refunded with $100,000 face amount of First and Refunding 4% Mortgage Bonds of Transportation Company, as authorized in Section 3 (a) (i) above, $100,100 face amount of additional Phila. & Willow Grove St. Ry. Co. 4½% Mtge. Bonds, due July 1, 1939 are held by the Trustee of the said sinking fund for said bonds. The bonds in said sinking fund will be owned by Transportation Company and not outstanding in the hands of the public but held by said sinking fund Trustee, and will be cancelled upon the retirement of said obligations which they will secure.

§These bonds are to remain outstanding, the collateral therefor to be exchanged for $2,333,400 face amount of 3%-6% Consolidated Mortgage Bonds of Transportation Company due January 1, 2039 described in Section 3 (b) above which will be owned by Transportation Company and not outstanding in the hands of the public but held by the Trustee for the Union Trac. Co. of Phila. 4% 50 Year Sinking Fund Collateral Trust Mtge. Bonds, due July 1, 1952, and will be cancelled upon the retirement of said obligations which they will secure.

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	Face Amount Outstanding in Hands of Public
(45) Peoples Passenger Railway Stock Trust Certificates	$4,150,000
(46) Electric and Peoples Traction Stock Trust Certificates	29,606,264

The Plan is conditioned upon its approval by two-thirds in amount of each such class of creditors.

(c) The rights of the following class are not modified or altered by the Plan; they are the holders of the following claims against the corporations set forth below or against property owned by them:

Mortgage Bonds	*Face Amount Outstanding in Hands of Public*
Continental Passenger Railway Company of Philadelphia First Mortgage 4% Bonds, due July 1, 1959	$280,000
Frankford and Southwark Philadelphia City Passenger Railroad Company, (Lombard and South Street Passenger Railway Company) First Mortgage 3½% Bonds, due December 1, 1951	150,000
Market Street Elevated Passenger Railway Company First Mortgage 4% Bonds, due May 1, 1955	10,000,000
Peoples Passenger Railway Company Second Mortgage 4% Bonds, due July 15, 1961	285,000
Peoples Passenger Railway Company Consolidated Mortgage 4% Bonds, due March 1, 1962	246,000
Philadelphia City Passenger Railway Company First Mortgage 4% Bonds, due January 1, 1960	200,000

	Face Amount Outstanding in Hands of Public
Philadelphia and Darby Railway Company, The, First Mortgage 5¾% Bonds, due May 1, 1957	$100,000
Philadelphia Rapid Transit Company Fifty Year 5% and 6% Sinking Fund Bonds, due March 1, 1962 (Second Mortgage on Market Street Subway-Elevated)	7,859,000†
Thirteenth and Fifteenth Streets Passenger Railway Company of the City of Philadelphia 6% First Mortgage Bonds, due January 1, 1944	436,000
Union Passenger Railway Company of Philadelphia First Mortgage 4% Bonds, due March 31, 1961	500,000
Union Passenger Railway Company of Philadelphia Second Mortgage 4% Bonds, due March 31, 1960	250,000
West Philadelphia Passenger Railway Company First Mortgage 3½% Bonds, due April 1, 1956	246,000
West Philadelphia Passenger Railway Company Second Mortgage 5½% Bonds, due May 1, 1956	750,000

Real Estate Mortgage Bonds	*Face Amount*
Motor Real Estate Company — Philadelphia Rapid Transit Company Real Estate First Mortgage 6% Bonds of C. Benton Cooper, due Jan. 1, 1944	$1,847,500*

* Estimated amount giving effect to estimated sinking fund retirements to January 1, 1939.

† $283,000 face amount additional P.R.T. Co. 50 Year 6% Sinking Fund Bonds due Mar. 1, 1962 will be owned by Transportation Company and not outstanding in the hands of the public but held by the Trustee of the sinking fund for the Phila. & Willow Grove St. Ry. Co. 4½% Mtge. Bonds due July 1, 1939; they will be cancelled when said obligations they will secure are retired.

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Real Estate Mortgages on following properties of Companies listed below

Motor Real Estate Company:	
Blanket Mortgage—Metropolitan Life Insurance Co.	$1,320,000
Rising Sun Ave. & Knorr St.	4,000
Venango, Wissahickon & Hunting Park Ave.	35,000
Mill Road, Upper Darby, Pa.	125,000
2nd & Erie Ave.	10,000
Penn & Comly Sts.	43,000
Front & Chew Sts.	246,157
251-53 S. 15th Street	65,000
Peoples Passenger Railway Company	
Pier 34 and East side Beach St.	62,600
Philadelphia Traction Company	
13th & Mt. Vernon Sts.	75,000
Union Traction Company of Philadelphia	
6739 Germantown Ave.	10,000

Ground Rents on the following properties of Companies listed below ¶

Electric Traction Company of Philadelphia	
Penn St.—So. of Laurel St.	$1,254
Frankford & Southwark Philadelphia City Passenger Railroad Company	
25th & South Sts.	5,010
25th & Lombard Sts.	2,500
Germantown Passenger Railway Company	
Taney St. No. of Poplar St.	3,347
27th & Poplar Sts.	733
2603 Poplar Street	10,000
Philadelphia City Passenger Railway Company	
Belmont Ave. & Jefferson St.	35,000
Philadelphia Traction Company	
Schuylkill Ave. So. of United States Naval Home	50,000
Real Estate Holding Company	
8 S. 33rd Street	333

¶ Ground rents which do not have a stated principal amount for redemption thereof are stated at an amount which represents a capitalization of the annual payments on a 6% basis.

SECTION 8. *City-Company Relationships.*

The Plan is conditioned upon the extension of the term of the Broad Street Subway System Lease to July 1, 1957. City action necessary to effect the foregoing and to evidence the City's necessary consents under the City-Company contract of July 1, 1907 will be seasonably sought.

SECTION 9. *Further Provisions of the Plan.*

(a) No executory contracts will be rejected under the Plan. Certain contracts, including the old leases and other inter-company contracts, will be terminated or revised by mutual consent in the formation by merger of Transportation Company.

(b) Reasonable compensation for services rendered and reimbursement for the actual and necessary expenses incurred in connection with the reorganization proceedings and the Plan, as may be duly authorized and approved by the Court, shall be paid in cash by Transportation Company.

(c) All claims incident to or arising out of the ordinary operation of the P.R.T. System, whether founded in contract or in tort, and including taxes, will, under the Plan, be paid in due course in cash.

(d) Under "The Contract of 1907" entered into between the City of Philadelphia and P.R.T. as of July 1, 1907, pursuant to Ordinance of City Council, the consent of the City, given by Ordinance of City Council, will be necessary to enable P.R.T. to take such steps as are necessary for the Plan to be consummated. Such consent will be seasonably sought.

(e) The plan will require prior approval by the Pennsylvania Public Utility Commission. Such approval will be seasonably sought.

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(f) Securities of Transportation Company will be exchanged, as set forth above, for the presently existing securities, against delivery of the latter by the holders thereof. In making said exchanges with each individual holder, bonds of less than $100 face amount and fractions of shares of Participating Preferred Stock or of Common Stock will not be issued; where a holder is entitled, whether or not in addition to whole pieces, to less than $100 in bonds and less than one share of stock, he will be issued scrip for such fractions of bonds or stock. Scrip for bonds will be issued only in amounts of one dollar or multiples thereof; and will be issued in such respective amounts as will be to the nearest dollar to which each individual holder will be entitled; that is to say, amounts from one to forty-nine cents will be dropped and for amounts of fifty to ninety-nine cents scrip for a whole dollar will be issued. Scrip for Participating Preferred Stock will be issued only in fractions of one twentieth of a share or multiples thereof; and will be issued in such respective amounts as will be to the nearest twentieth of a share to which each individual holder will be entitled; that is to say, amounts up to one-half of one twentieth of a share will be dropped and for amounts of one-half or more of one twentieth of a share scrip for a whole one twentieth of a share will be issued. Scrip for Common Stock will be issued only in fractions of one-half of a share, this being the only fraction involved in the case of Common Stock. No interest will be paid on scrip for bonds and said scrip will not be deemed to be bonds and the holders thereof will not be deemed to be bondholders or to have any of the rights thereof, until said scrip is converted into bonds. Scrip for bonds will be converted into bonds of not less than $100 face amount against delivery of scrip in sufficient amounts. No dividends will be paid on scrip for Participating Preferred Stock or Common Stock, and said scrip will not be deemed to be stock and the holders thereof will not be deemed to be stockholders or to have any of the rights thereof, until said

scrip is converted into stock certificates for whole shares. Scrip for stock will be converted into stock certificates for whole shares against delivery of scrip in sufficient amounts. Such conversion of scrip for bonds or stock must be made on or before December 31, 1943 and after said date all unconverted scrip will be void and of no value whatever.

(g) The execution of the Plan shall be carried out in the manner set forth in the Plan and pursuant to the provisions of the Federal Bankruptcy Act. Reorganization managers may be appointed with the approval of the Court. The detailed means and methods to be taken to present the Plan to the security holders who will be entitled to vote thereon, and of obtaining the necessary acceptances, consents and approvals of the Plan to secure its confirmation and consummation, shall be determined, subject to the provisions of the Plan and of the Federal Bankruptcy Act, by such reorganization managers and they shall take or cause to be taken such steps and action as they shall so determine to be necessary or desirable to secure the required acceptances, consents, approvals and confirmation of the Plan and in order to carry out the Plan after its confirmation. The form of all new securities to be issued under the Plan, and of all instruments and documents contemplated thereby or necessary or proper in connection therewith, shall be determined with the approval of the reorganization managers, subject to such final approvals as are requisite under the provisions of the Plan and of the Federal Bankruptcy Act. All steps taken shall be subject to such approval of the Court as may be required. The reorganization managers shall endeavor to carry out the reorganization in accordance with the Plan and subject to the supervision of the Court, but shall not assume any personal liability in connection with carrying out the Plan, except to exercise good faith in such endeavor.

(h) The reorganization of the corporations parties to the Plan shall, upon final approval and confirmation, be and become effective as of January 1, 1939.

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SCHEDULE "A"

COMPANIES TO MERGE IN ADDITION TO PARTIES TO THE PLAN.

Companies, all the stock of which is owned by P.R.T.:

Broad Street and Boulevard Street Railway Company,
Broad Street Rapid Transit Street Railway Company,
Bustleton and Byberry Rapid Transit Street Railway Company,
Cayuga and Torresdale Street Railway Company,
Champlost Street Connecting Railway Company,
Frankford Connecting Railway Company,
Germantown Loop Railway Company,
Glenwood Rapid Transit Street Railway Company,
Mount Vernon, Shawmont and Roxborough Street Railway Company,
Moyamensing and Southwark Rapid Transit Street Railway Company,
Parkside Rapid Transit Street Railway Company,
Pelham and Frankford Street Railway Company,
Sansom Street Connecting Railway Company,
Tioga and Frankford Street Railway Company,
Wayne Junction Connecting Railway Company.

Companies, all the stock of which is owned by Union Traction Company of Philadelphia:

Aramingo Avenue Passenger Railway Company, The,
Beach Street Connecting Railway Company,
Brown and Parrish Street Railway Company, The,
Centennial Passenger Railway Company, The,
Citizens Clearfield and Cambria Street Railway Company, The,
Citizens East End Street Railway Company, The,
Citizens North End Street Railway Company, The,
East Aramingo Avenue Passenger Railway Company, The,
Girard Avenue Passenger Railway Company, The,

Hillcrest Avenue Passenger Railway Company,
Lehigh Avenue Railway Company of Philadelphia,
Northern Passenger Railway Company, The,
Philadelphia, Cheltenham and Jenkintown Passenger Railway Company, The,
Snyder Avenue Railway Company.

Companies, all the stock of which is owned as follows:

Fairmount Park Railway Company, The
(100% owned by Thirteenth and Fifteenth Streets Passenger Railway Company),
Huntingdon Street Connecting Passenger Railway Company
(100% owned by Philadelphia Traction Company),
Kessler Street Connecting Passenger Railway Company
(100% owned by Philadelphia Traction Company),
Park Avenue and Carlisle Street Passenger Railway Company of Philadelphia, The
(100% owned by Thirteenth and Fifteenth Streets Passenger Railway Company),
Ridge Avenue Connecting Railway Company
(100% owned by Philadelphia Traction Company),
Tioga and Venango Streets Passenger Railway Company of Philadelphia, The
(100% owned by Thirteenth and Fifteenth Streets Passenger Railway Company),
Twenty-Second Street and Allegheny Avenue Passenger Railway Company
(89% owned by Philadelphia Traction Company, 11% owned by Union Traction Company of Philadelphia),
Walnut Street Connecting Passenger Railway Company of the City of Philadelphia, The
(100% owned by Philadelphia Traction Company).

NOTE: As a part of the Plan, and either prior to or subsequent to said merger, all of the corporate powers,

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franchises, property, rights and credits of Philadelphia Rural Transit Company and Pennsylvania Rapid Transit Company will be acquired by P.R.T. or its successor, Transportation Company, and those of D M & C Bus Company will be acquired by Darby, Media and Chester Street Railway Company or its successor, Transportation Company, as set forth in Section 2 above.

SCHEDULE "B"

COMPANIES NOT TO BE MERGED, ALL THE STOCK OF WHICH EXCEPT AS NOTED WILL BE OWNED BY TRANSPORTATION COMPANY.

Chester and Philadelphia Railway Company (51 per cent. of stock will be owned by Transportation Company),
Market Street Elevated Passenger Railway Company,
Motor Real Estate Company,
Real Estate Holding Company,
Willow Grove Park Company.

SCHEDULE "C"

PRIOR LIEN BONDS, MORTGAGES AND GROUND RENTS TO REMAIN OUTSTANDING AND WHICH MAY BE LATER REFUNDED BY THE ISSUE OF PHILADELPHIA TRANSPORTATION COMPANY BONDS.

Continental Passenger Railway Company of Philadelphia First Mortgage 4% Bonds, due July 1, 1959	$280,000
Frankford & Southwark Philadelphia City Passenger Railroad Company, (Lombard & South Street Passenger Railway Company) First Mortgage 3½% Bonds, due December 1, 1951	150,000
Market Street Elevated Passenger Railway Company First Mortgage 4% Bonds, due May 1, 1955	10,000,000

Peoples Passenger Railway Company Second Mortgage 4% Bonds, due July 15, 1961	$285,000
Peoples Passenger Railway Company consolidated Mortgage 4% Bonds, due March 1, 1962	246,000
Philadelphia City Passenger Railway Company First Mortgage 4% Bonds, due January 1, 1960	200,000
Philadelphia & Darby Railway Company, The, First Mortgage 5¾% Bonds, due May 1, 1957	100,000
Philadelphia Rapid Transit Company 5% Collateral Bonds, due February 1, 1957	2,107,000*
Philadelphia Rapid Transit Company 50 Year 5% and 6% Sinking Fund Bonds, due March 1, 1962 (Second Mortgage on Market Street Subway-Elevated)	7,859,000†
Philadelphia and Willow Grove Street Railway Company 4½% Mortgage Bonds, due July 1, 1939	363,300†
Thirteenth and Fifteenth Streets Passenger Railway Company of the City of Philadelphia 6% First Mortgage Bonds, due January 1, 1944	436,000
Union Passenger Railway Company of Philadelphia First Mortgage 4% Bonds, due March 31, 1961	500,000
Union Passenger Railway Company of Philadelphia Second Mortgage 4% Bonds, due March 31, 1960	250,000
Union Traction Company of Philadelphia 4% 50 Year Sinking Fund Collateral Trust Mortgage Bonds, due July 31, 1952	523,000
West Philadelphia Passenger Railway Company First Mortgage 3½% Bonds, due April 1, 1956	246,000

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West Philadelphia Passenger Railway Company Second Mortgage 5½% Bonds, due May 1, 1956	$750,000
Real Estate Mortgage Bonds and Miscellaneous Real Estate Mortgages and Ground Rents (Schedule E-1)	3,951,435
TOTAL	$28,246,735*†

*Estimated amount giving effect to estimated sinking fund retirements to January 1, 1939.

†$283,000 face amount additional P.R.T. 50 Year 6% Sinking Fund Bonds due Mar. 1, 1962 and $100,100 face amount additional Phila. & Willow Grove St. Ry. Co. 4½% Mtge. Bonds due July 1, 1939 will be owned by Transportation Company and not outstanding in the hands of the public but held by the Trustee of the sinking fund for said Phila. & Willow Grove St. Ry. Co. Bonds; they will be cancelled when said obligations they will secure are retired.

SCHEDULE "D"

DISTRIBUTION OF SECURITIES OF PHILADELPHIA TRANSPORTATION COMPANY AND CASH TO BE ISSUED IN E
OF LESSOR COMPANIES OUTSTANDING IN THE HANDS OF THE

NEW SECURITIES* AND CASH TO BE RECEIVED IN EXCHANGE FOR OLD STOCK AND STOCK TRUST CERTIFIC

CLASS "A"	Old Shares or Stk. Tr. Ctfs. Outstanding in Hands of Public	Securities: 3⅞-6% Consolidated Mortgage Bonds — Face Value: Total	3⅞-6% Consolidated Mortgage Bonds — Face Value: Per Old Share or Stk Tr Ctf	Participating Preferred Stock‡ — Shares: Total	Participating Preferred Stock‡ — Shares: Per Old Share or Stk Tr Ctf	Participating Preferred Stock‡ — Par Value: Total	Participating Preferred Stock‡ — Par Value: Per Old Share or Stk Tr Ctf	Total Face and Par Value of New Securities: Total	Total Face and Par Value of New Securities: Per Old Share or Stk Tr Ctf	T C
Citizens Passenger Railway Co. of Philadelphia	10,000	$1,008,500.00	$100.85	8,450.0	0.845	$169,000.00	$16.90	$1,177,500.00	$117.75	$
Continental Passenger Railway Co. of Philadelphia	20,000	749,200.00	37.46	6,270.0	0.3135	125,400.00	6.27	874,600.00	43.73	
Fairmount Park & Haddington Passenger Railway Co., The	6,000	129,660.00	21.61	1,086.0	0.181	21,720.00	3.62	151,380.00	25.23	
Frankford & Southwark Philadelphia City Passenger Railroad Co.	37,500	4,862,625.00	129.67	40,725.0	1.086	814,500.00	21.72	5,677,125.00	151.39	1
Germantown Passenger Railway Co.	30,000	1,134,600.00	37.82	9,495.0	0.3165	189,900.00	6.33	1,324,500.00	44.15	
Green & Coates Streets Philadelphia Passenger Railway Co.	10,000	432,300.00	43.23	3,620.0	0.362	72,400.00	7.24	504,700.00	50.47	
Philadelphia City Passenger Railway Co.	19,919	1,076,223.57	54.03	9,003.4	0.452	180,068.00	9.04	1,256,291.57	63.07	
Philadelphia & Darby Railway Co., The	3,295	39,408.20	11.96	329.5	0.1	6,590.00	2.00	45,998.20	13.96	
Philadelphia & Grays Perry Passenger Railway Co.	12,296	354,370.72	28.82	2,963.3	0.241	59,266.00	4.82	413,636.72	33.64	
Ridge Avenue Passenger Railway Co.	15,000	1,296,750.00	86.45	10,852.5	0.7235	217,050.00	14.47	1,513,800.00	100.92	
Second & Third Streets Passenger Railway Co. of Philadelphia	21,204	1,833,085.80	86.45	15,341.1	0.7235	306,822.00	14.47	2,139,907.80	100.92	
Thirteenth & Fifteenth Sts. Passenger Railway Co. of the City of Philadelphia	19,950	1,724,677.50	86.45	14,433.8	0.7235	288,676.00	14.47	2,013,353.50	100.92	
Union Passenger Railway Co. of Philadelphia	23,954	1,416,879.10	59.15	11,857.2	0.495	237,144.00	9.90	1,654,023.10	69.05	
West Philadelphia Passenger Railway Co.	7,141	445,027.12	62.32	3,724.0	0.5215	74,480.00	10.43	519,507.12	72.75	
Peoples Passenger Railway Co. Stock Trust Certificates	4,150-A	1,195,864.00	288.16	10,016.0	2.4135	200,320.00	48.27	1,396,184.00	336.43	
Total Class "A"	.....	$17,699,171.01	.....	148,166.8	.....	$2,963,336.00	.....	$20,662,507.01	.....	$
CLASS "B"										
Hestonville, Mantua & Fairmount Passenger Railroad										

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SCHEDULE "D"

RANSPORTATION COMPANY AND CASH TO BE ISSUED IN EXCHANGE FOR STOCK AND STOCK TRUST CERTIFICATES
LESSOR COMPANIES OUTSTANDING IN THE HANDS OF THE PUBLIC

CASH TO BE RECEIVED IN EXCHANGE FOR OLD STOCK AND STOCK TRUST CERTIFICATES

Securities					Cash		Annual Return on 3%-6% Consolidated Mortgage Bonds†				Participating Preferred Stock
Participating Preferred Stock‡			Total Face and Par Value of New Securities				3% (Fixed)		6% (Maximum) (Additional 3% if earned)		
hares	Par Value										Preference Dividend (if earned)
Per Old Share or Stk Tr Ctf	Total	Per Old Share or Stk Tr Ctf	Total	Per Old Share or Stk Tr Ctf	Total Cash	Cash Per Old Share or Stk Tr Ctf	Total	Per Old Share or Stk Tr Ctf	Total	Per Old Share or Stk Tr Ctf	Per Old Share or Stk Tr Ctf‡
0.845	$169,000.00	$16.90	$1,177,500.00	$117.75	$35,000.00	$3.50	$30,255.00	$3.03	$60,510.00	$6.05	$0.85
0.3135	125,400.00	6.27	874,600.00	43.73	26,000.00	1.30	22,476.00	1.12	44,952.00	2.25	.31
0.181	21,720.00	3.62	151,380.00	25.23	3,000.00	.50	3,889.80	.65	7,779.60	1.30	.18
1.086	814,500.00	21.72	5,677,125.00	151.39	168,750.00	4.50	145,878.75	3.89	291,757.50	7.78	1.09
0.3165	189,900.00	6.33	1,324,500.00	44.15	39,300.00	1.31	34,038.00	1.13	68,076.00	2.27	.32
0.362	72,400.00	7.24	504,700.00	50.47	15,000.00	1.50	12,969.00	1.30	25,938.00	2.59	.36
0.452	180,068.00	9.04	1,256,291.57	63.07	37,447.72	1.88	32,286.71	1.62	64,573.41	3.24	.45
0.1	6,590.00	2.00	45,998.20	13.96	1,383.90	.42	1,182.25	.36	2,364.49	.72	.10
0.241	59,266.00	4.82	413,636.72	33.64	12,296.00	1.00	10,631.12	.86	21,262.24	1.73	.24
0.7235	217,050.00	14.47	1,513,800.00	100.92	15,000.00	1.00	38,902.50	2.59	77,805.00	5.19	.72
0.7235	306,822.00	14.47	2,139,907.80	100.92	63,612.00	3.00	54,992.57	2.59	109,985.15	5.19	.72
0.7235	288,676.00	14.47	2,013,353.50	100.92	59,850.00	3.00	51,740.33	2.59	103,480.65	5.19	.72
0.495	237,144.00	9.90	1,654,023.10	69.05	49,105.70	2.05	42,506.37	1.77	85,012.75	3.55	.50
0.5215	74,480.00	10.43	519,507.12	72.75	15,424.56	2.16	13,350.81	1.87	26,701.63	3.74	.52
2.4135	200,320.00	48.27	1,396,184.00	336.43	27,680.50	6.67	35,875.92	8.64	71,751.84	17.29	2.41
.....	$2,963,336.00	.....	$20,662,507.01	.....	$568,850.38	.....	$530,975.13	.....	$1,061,950.26	.....	.....
0.207	$16,676.00	$4.14	$50,591.76	$12.56	$2,014.00	$0.50	$1,017.47	$0.25	$2,034.95	$0.51	$0.21
0.3115	36,744.00	6.23	111,353.70	18.88	4,423.50	.75	2,238.29	.38	4,476.58	.76	.31
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

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Class "A"	Old Shares or Stk. Tr. Ctfs. Outstanding in Hands of Public	Face Value		Shares		Par Value			
		Total	Per Old Share or Stk Tr Ctf	Total	Per Old Share or Stk Tr Ctf	Total	Per Old Share or Stk Tr Ctf	Total	Per Old Share or Stk Tr Ctf
Citizens Passenger Railway Co. of Philadelphia	10,000	$1,008,500.00	$100.85	8,450.0	0.845	$169,000.00	$16.90	$1,177,500.00	$117.75
Continental Passenger Railway Co. of Philadelphia	20,000	749,200.00	37.46	6,270.0	0.3135	125,400.00	6.27	874,600.00	43.73
Fairmount Park & Haddington Passenger Railway Co., The	6,000	129,660.00	21.61	1,086.0	0.181	21,720.00	3.62	151,380.00	25.23
Frankford & Southwark Philadelphia City Passenger Railroad Co.	37,500	4,862,625.00	129.67	40,725.0	1.086	814,500.00	21.72	5,677,125.00	151.39
Germantown Passenger Railway Co.	30,000	1,134,600.00	37.82	9,495.0	0.3165	189,900.00	6.33	1,324,500.00	44.15
Green & Coates Streets Philadelphia Passenger Railway Co.	10,000	432,300.00	43.23	3,620.0	0.362	72,400.00	7.24	504,700.00	50.47
Philadelphia City Passenger Railway Co.	19,919	1,076,223.57	54.03	9,003.4	0.452	180,068.00	9.04	1,256,291.57	63.07
Philadelphia & Darby Railway Co., The	3,295	39,408.20	11.96	329.5	0.1	6,590.00	2.00	45,998.20	13.96
Philadelphia & Grays Ferry Passenger Railway Co.	12,296	354,370.72	28.82	2,963.3	0.241	59,266.00	4.82	413,636.72	33.64
Ridge Avenue Passenger Railway Co.	15,000	1,296,750.00	86.45	10,852.5	0.7235	217,050.00	14.47	1,513,800.00	100.92
Second & Third Streets Passenger Railway Co. of Philadelphia	21,204	1,833,085.80	86.45	15,341.1	0.7235	306,822.00	14.47	2,139,907.80	100.92
Thirteenth & Fifteenth Sts. Passenger Railway Co. of the City of Philadelphia	19,950	1,724,677.50	86.45	14,433.8	0.7235	288,676.00	14.47	2,013,353.50	100.92
Union Passenger Railway Co. of Philadelphia	23,954	1,416,879.10	59.15	11,857.2	0.495	237,144.00	9.90	1,654,023.10	69.05
West Philadelphia Passenger Railway Co.	7,141	445,027.12	62.32	3,724.0	0.5215	74,480.00	10.43	519,507.12	72.75
Peoples Passenger Railway Co. Stock Trust Certificates	4,150-A	1,195,864.00	288.16	10,016.0	2.4135	200,320.00	48.27	1,396,184.00	336.43
Total Class "A"	.....	$17,699,171.01	.....	148,166.8	.....	$2,963,336.00	.....	$20,662,507.01	.....
Class "B"									
Hestonville, Mantua & Fairmount Passenger Railroad Co.:									
Common	4,028	$33,915.76	$8.42	833.8	0.207	$16,676.00	$4.14	$50,591.76	$12.56
Preferred	5,898	74,609.70	12.65	1,837.2	0.3115	36,744.00	6.23	111,353.70	18.88
Philadelphia Traction Co.	400,000	6,728,000.00	16.82	166,000.0	0.415	3,320,000.00	8.30	10,048,000.00	25.12
Electric & Peoples Traction Stock Trust Certificates	29,606-B	4,980,365.73	168.22	122,777.2	4.147	2,455,544.00	82.94	7,435,909.73	251.16
Total Class "B"	.....	$11,816,891.19	.....	291,448.2	.....	$5,828,964.00	.....	$17,645,855.19	.....
Class "C"									
Union Traction Co. of Philadelphia	598,979	$2,407,895.58	$4.02	171,907.0	0.287	$3,438,140.00	$5.74	$5,846,035.58	$9.76
Darby, Media & Chester Street Railway Co.	17,000	49,640.00	2.92	3,544.5	0.2085	70,890.00	4.17	120,530.00	7.09
Total Class "C"	.....	$2,457,535.58	.....	175,451.5	.....	$3,509,030.00	.....	$5,966,565.58	.....
Summary Totals	.....	$31,973,597.78	.....	615,066.5	.....	$12,301,330.00	.....	$44,274,927.78	.....

NOTES: A—$1,000 Peoples Passenger Railway Stock Trust Certificates.
B—$1,000 Electric and Peoples Traction Stock Trust Certificates.
*—See Section 9 (f) as to fractions.
†—See Section 3 (d) as to return on new Participating Preferred Stock.
‡—See Section 3 (b) as to interest on Consolidated Mortgage Bonds.

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Securities					Cash		Annual Return on 3%-6% Consolidated Mortgage Bonds†				Participating Preferred Stock
Participating Preferred Stock‡			Total Face and Par Value of New Securities				3% (Fixed)		6% (Maximum) (Additional 3% if earned)		
hares	Par Value										Preference Dividend (if earned)
Per Old Share or Stk Tr Ctf	Total	Per Old Share or Stk Tr Ctf	Total	Per Old Share or Stk Tr Ctf	Total Cash	Cash Per Old Share or Stk Tr Ctf	Total	Per Old Share or Stk Tr Ctf	Total	Per Old Share or Stk Tr Ctf	Per Old Share or Stk Tr Ctf‡
0.845	$169,000.00	$16.90	$1,177,500.00	$117.75	$35,000.00	$3.50	$30,255.00	$3.03	$60,510.00	$6.05	$0.85
0.3135	125,400.00	6.27	874,600.00	43.73	26,000.00	1.30	22,476.00	1.12	44,952.00	2.25	.31
0.181	21,720.00	3.62	151,380.00	25.23	3,000.00	.50	3,889.80	.65	7,779.60	1.30	.18
1.086	814,500.00	21.72	5,677,125.00	151.39	168,750.00	4.50	145,878.75	3.89	291,757.50	7.78	1.09
0.3165	189,900.00	6.33	1,324,500.00	44.15	39,300.00	1.31	34,038.00	1.13	68,076.00	2.27	.32
0.362	72,400.00	7.24	504,700.00	50.47	15,000.00	1.50	12,969.00	1.30	25,938.00	2.59	.36
0.452	180,068.00	9.04	1,256,291.57	63.07	37,447.72	1.88	32,286.71	1.62	64,573.41	3.24	.45
0.1	6,590.00	2.00	45,998.20	13.96	1,383.90	.42	1,182.25	.36	2,364.49	.72	.10
0.241	59,266.00	4.82	413,636.72	33.64	12,296.00	1.00	10,631.12	.86	21,262.24	1.73	.24
0.7235	217,050.00	14.47	1,513,800.00	100.92	15,000.00	1.00	38,902.50	2.59	77,805.00	5.19	.72
0.7235	306,822.00	14.47	2,139,907.80	100.92	63,612.00	3.00	54,992.57	2.59	109,985.15	5.19	.72
0.7235	288,676.00	14.47	2,013,353.50	100.92	59,850.00	3.00	51,740.33	2.59	103,480.65	5.19	.72
0.495	237,144.00	9.90	1,654,023.10	69.05	49,105.70	2.05	42,506.37	1.77	85,012.75	3.55	.50
0.5215	74,480.00	10.43	519,507.12	72.75	15,424.56	2.16	13,350.81	1.87	26,701.63	3.74	.52
2.4135	200,320.00	48.27	1,396,184.00	336.43	27,680.50	6.67	35,875.92	8.64	71,751.84	17.29	2.41
.....	$2,963,336.00	.....	$20,662,507.01	.....	$568,850.38	.....	$530,975.13	.....	$1,061,950.26	.....	.....
0.207	$16,676.00	$4.14	$50,591.76	$12.56	$2,014.00	$0.50	$1,017.47	$0.25	$2,034.95	$0.51	$0.21
0.3115	36,744.00	6.23	111,353.70	18.88	4,423.50	.75	2,238.29	.38	4,476.58	.76	.31
0.415	3,320,000.00	8.30	10,048,000.00	25.12	800,000.00	2.00	201,840.00	.50	403,680.00	1.01	.42
4.147	2,455,544.00	82.94	7,435,909.73	251.16	592,125.28	20.00	149,410.97	5.05	298,821.94	10.09	4.15
.....	$5,828,964.00	.....	$17,645,855.19	.....	$1,398,562.78	.....	$354,506.73	.....	$709,013.47	.....	.....
0.287	$3,438,140.00	$5.74	$5,846,035.58	$9.76	$227,612.02	$0.38	$72,236.87	$0.12	$144,473.74	$0.24	$0.29
0.2085	70,890.00	4.17	120,530.00	7.09	9,180.00	.54	1,489.20	.09	2,978.40	.18	.21
.....	$3,509,030.00	.....	$5,966,565.58	.....	$236,792.02	.....	$73,726.07	.....	$147,452.14	.....	.....
.....	$12,301,330.00	.....	$44,274,927.78	.....	$2,204,205.18	.....	$959,207.93	.....	$1,918,415.87	.....	.....

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SCHEDULE "E"

CAPITAL SECURITIES TO BE OUTSTANDING UPON EFFECTUATION OF THE PLAN.

Real Estate Mortgage Bonds and Miscellaneous Real Estate Mortgages and Ground Rents	Schedule E-1		$3,951,435.64
Collateral Trust Bonds	Schedule E-2		2,630,000.00
Divisional Lien Bonds	Schedule E-3		21,665,300.00*
Philadelphia Transportation Company First and Refunding Mortgage 4% Bonds	Schedule E-4		1,897,860.00*
Philadelphia Transportation Company 3%-6% Consolidated Mortgage Bonds	Schedule E-5		
For stock and stock trust certificates of Lessor Companies		$31,973,597.78	
For refunding certain bonds of Lessor Companies		596,400.00	
			32,569,997.78†
			$62,714,593.52
Philadelphia Transportation Company Participating Preferred Stock (755,067 shares, par value $20 per share)			$15,101,340.00
Philadelphia Transportation Company Common Stock (719,926 shares, no par value, with a stated value of $10 per share)			7,199,260.00
			$22,300,600.00
TOTAL			$85,015,193.42*†

*$383,100 face amount additional Divisional Lien Bonds and $100,000 face amount additional First and Refunding 4% Mortgage Bonds will be owned by Transportation Company and not outstanding in the hands of the public but held by the Trustee of the sinking fund for the Phila. & Willow Grove St. Ry. Co. 4½% Mtge. Bonds, due uly 1, 1939; they will be cancelled when said obligations they will secure are retired.

†$11,810,100 face amount additional 3%-6% Consolidated Mortgage Bonds will be issued in exchange of collateral security for the collateral trust bonds listed in Echedule "E-2"; said additional Consolidated Mortgage Bonds will be owned by Transportation Company and not outstanding in the hands of the public but held by the Trustee of said collateral trust bonds; they will be cancelled when the obligations they will secure are retired.

SCHEDULE "E-1"

REAL ESTATE MORTGAGE BONDS AND MISCELLANEOUS REAL ESTATE MORTGAGES AND GROUND RENTS OUTSTANDING JANUARY 1, 1939, ON PROPERTY OF COMPANIES MENTIONED BELOW.

Company	*Due*	*Interest Rate*	*Amount*
Real Estate Mortgage Bonds			
Motor Real Estate Company			
Philadelphia Rapid Transit Company Real Estate First Mortgage 6% Bonds of C. Benton Cooper	Jan. 1, 1944	6%	$1,847,500.00*
Real Estate Mortgages			
Motor Real Estate Company			
Blanket Mortgage—Metropolitan Life Insurance Co.	Mar. 1, 1951	6	$1,320,000.00
Rising Sun Ave. & Knorr St.	Overdue	6	4,000.00
Venango, Wissahickon & Hunting Park Ave.	Overdue	6	35,000.00
Mill Road, Upper Darby, Pa.	Overdue	6	125,000.00
2nd & Erie Ave.	Dec. 13, 1940	4.5	10,000.00
Penn & Comly Sts.	Callable on 3 mo. notice	6	43,000.00
Front & Chew Sts.	Overdue	6	246,157.00
251-53 S. 15th Street	Overdue	5.5	65,000.00
Peoples Passenger Railway Company			
Pier 34 and E. side Beach St.	Overdue	6	62,600.00
Philadelphia Traction Company			
13th & Mt. Vernon Sts.	Overdue	6	75,000.00
Union Traction Company of Philadelphia			
6739 Germantown Ave.	Overdue	6	10,000.00
TOTAL MORTGAGES			$1,995,757.00
Ground Rents¶			
Electric Traction Company of Philadelphia			
Penn St.—S. of Laurel St.	.....	6	$1,254.16
Frankford & Southwark Philadelphia City Passenger Railroad Company			
25th & South Sts.	.....	6	5,010.00
25th & Lombard Sts.	.....	6	2,500.00

* Estimated amount giving effect to estimated sinking fund returements to January 1, 1939.

¶ Ground rents which do not have a stated principal amount for redemption thereof are stated at an amount which represent a capitalization of the annual payments on a 6% basis.

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Ground Rents¶			
Germantown Passenger Railway Company			
Taney St. No. of Poplar St.	.....	6	$3,347.80
27th & Poplar Sts.	.....	6	733.34
2603 Poplar Street	.....	5	10,000.00
Philadelphia City Passenger Railway Company			
Belmont Ave. & Jefferson St.	Sept. 1, 1939	4	35,000.00
Philadelphia Traction Company			
Schuylkill Ave. So. of United States Naval Home	.....	5	50,000.00
Real Estate Holding Company			
8 S. 33rd Street	.....	6	333.34
TOTAL GROUND RENTS			$108,178.64
TOTAL			$3,951,435.64*

SCHEDULE "E-2"

COLLATERAL TRUST BONDS OUTSTANDING JANUARY 1, 1939.

Philadelphia Rapid Transit Company 5% Collateral Bonds, due February 1, 1957	$2,107,000*†
Union Traction Company of Philadelphia 4% 50-Year Sinking Fund Collateral Trust Mortgage Bonds, due July 1, 1952	523,000†
TOTAL	$2,630,000*†

*Estimated amount giving effect to estimated sinking fund retirements to January 1, 1939.

¶ Ground rents which do not have a stated principal amount for redemption thereof are stated at an amount which represents a capitalization of the annual payments on a 6% basis.

† In exchange for the collateral security now held by the Trustees of the aforesaid Collateral Trust Bonds, there will be issued 3%-6% Consolidated Mortgage Bonds of Transportation Company due January 1, 2039, described in Section 3 (b) above, as follows: (1) to the Trustee of $2,107,000 face amount of Philadelphia Rapid Transit Company 5% Collateral Bonds due February 1, 1957 outstanding, in exchange for said existing collateral security therefor, $9,476,700 face amount of said 3%-6% Consolidated Mortgage Bonds; and (2) to the Trustee of $523,000 face amount of Union Traction Company of Philadelphia 4% Sinking Fund Collateral Trust Mortgage Bonds due July 1, 1952, outstanding, in exchange for said existing collateral security therefor, $2,333,400 face amount of said 3%-6% Consolidated Mortgage Bonds. These said additional Consolidated Mortgage Bonds, which will be in the total face amount of $11,810,100, will be owned by Transportation Company and not outstanding in the hands of the public but held by the Trustees for the aforesaid collateral trust bonds as collateral security therefor; the said two respective amounts of said Consolidated Mortgage Bonds are in such amount that the fixed interest thereon would equal the interest and sinking fund payments required by the indentures under which the aforesaid respective collateral trust bonds were issued. Such Consolidated Mortgage Bonds shall be cancelled upon the retirement of the said respective obligations which they will secure.

SCHEDULE "E-3"

DIVISIONAL LIEN BONDS OUTSTANDING JANUARY 1, 1939.

Continental Passenger Railway Company of Philadelphia First Mortgage 4% Bonds, due July 1, 1959	$280,000
Frankford & Southwark Philadelphia City Passenger Railroad Company, (Lombard & South Street Passenger Railway Company) First Mortgage 3½% Bonds, due December 1, 1951	150,000
Market Street Elevated Passenger Railway Company First Mortgage 4% Bonds, due May 1, 1955	10,000,000
Peoples Passenger Railway Company Second Mortgage 4% Bonds, due July 15, 1961	285,000
Peoples Passenger Railway Company Consolidated Mortgage 4% Bonds, due March 1, 1962	246,000
Philadelphia City Passenger Railway Company First Mortgage 4% Bonds, due January 1, 1960	200,000
Philadelphia & Darby Railway Company, The, First Mortgage 5¾% Bonds, due May 1, 1957	100,000
Philadelphia Rapid Transit Company 50-Year 5% and 6% Sinking Fund Bonds, due March 1, 1962 (Second Mortgage on Market Street Subway-Elevated)	7,859,000†
Philadelphia and Willow Grove Street Railway Company 4½% Mortgage Bonds, due July 1, 1939	363,300†

†$283,000 face amount additional of P.R.T. Co. 50 Year 6% Sinking Fund Bonds due Mar. 1, 1962 and $100,100 face amount additional Phila. & Willow Grove St. Ry. Co. 4½% Mtge. Bonds due July 1, 1939 will be owned by Transportation Company and not outstanding in the hands of the public but held by the Trustee of the sinking fund for said Phila. & Willow Grove St. Ry. Co. bonds; they will be cancelled when said obligations they secure are retired.

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Thirteenth and Fifteenth Streets Passenger Railway Company of the City of Philaphia 6% First Mortgage Bonds, due January 1, 1944	$436,000
Union Passenger Railway Company of Philadelphia First Mortgage 4% Bonds, due March 31, 1961	500,000
Union Passenger Railway Company of Philadelphia Second Mortgage 4% Bonds, due March 31, 1960	250,000
West Philadelphia Passenger Railway Company First Mortgage 3½% Bonds, due April 1, 1956	246,000
West Philadelphia Passenger Railway Company Second Mortgage 5½% Bonds, due May 1, 1956	750,000
TOTAL	$21,665,300†

SCHEDULE "E-4"

PHILADELPHIA TRANSPORTATION COMPANY FIRST AND REFUNDING MORTGAGE 4% BONDS OUTSTANDING JANUARY 1, 1939.

Issued to Holders of

Darby and Yeadon Street Railway Company 4½% First Mortgage Bonds, due December 1, 1934	$200,000
Peoples Passenger Railway Company First Mortgage 4% Bonds, due January 15, 1935	219,000
Philadelphia City Passenger Railway Company 5% Debenture Coupon Bonds, due March 1, 1935	100,000

†$283,000 face amount additional of P.R.T. Co. 50 Year 6% Sinking Fund Bonds due Mar. 1, 1962 and $100,100 face amount additional Phila. & Willow Grove St. Ry. Co. 4½% Mtge. Bonds due July 1, 1939 will be owned by Transportation Company and not outstanding in the hands of the public but held by the Trustee of the sinking fund for said Phila. & Willow Grove St. Ry. Co. bonds; they will be cancelled when said obligations they secure are retired.

Empire Passenger Railway Company of Philadelphia 6% First Mortgage Bonds, due March 1, 1935	$100,000*
Catherine & Bainbridge Streets Railway Company of the City of Philadelphia, The, First Mortgage 6% Bonds, due April 1, 1935	150,000
Frankford & Southwark Philadelphia City Passenger Railroad Company, (West End Passenger Railway Company) First Mortgage 4% Bonds, due October 1, 1935	132,100
Hestonville, Mantua & Fairmount Passenger Railroad Company 5½% Consolidated Bonds, due May 1, 1934 and May 1, 1939	896,760
Seventeenth & Nineteenth Streets Passenger Railway Company of Philadelphia First Mortgage 6% Bonds, due July 1, 1939	100,000
Total to be presently issued for refunding	$1,897,860*

SCHEDULE "E-5"

PHILADELPHIA TRANSPORTATION COMPANY 3%-6% CONSOLIDATED MORTGAGE BONDS OUTSTANDING JANUARY 1, 1939.

Issued to holders of the following stocks and stock trust certificates:

Citizens Passenger Railway Company of Philadelphia	$1,008,500.00
Continental Passenger Railway Company of Philadelphia	749,200.00

*$100,000 face amount additional First and Refunding 4% Mortgage Bonds will be issued in exchange for $100,000 face amount additional Empire Pass. Ry. Co. of Phila. 6% 1st Mtge. Bonds, due Mar. 1, 1935; they will be owned by Transportation Company and not outstanding in the hands of the public but held by the Trustee of the sinking fund for the Phila. & Willow Grove St. Ry. Co. 4½% Mtge. Bonds due July 1, 1939; they will be cancelled when said obligations they secure are retired.

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Fairmount Park & Haddington Passenger Railway Company, The	$129,660.00
Frankford & Southwark Philadelphia City Passenger Railroad Company	4,862,625.00
Germantown Passenger Railway Company	1,134,600.00
Green & Coates Streets Philadelphia Passenger Railway Company	432,300.00
Philadelphia City Passenger Railway Company	1,076,223.57
Philadelphia & Darby Railway Company, The	39,408.20
Philadelphia & Grays Ferry Passenger Railway Company	354,370.72
Ridge Avenue Passenger Railway Company	1,296,750.00
Second & Third Streets Passenger Railway Company of Philadelphia	1,833,085.80
Thirteenth & Fifteenth Streets Passenger Railway Company of the City of Philadelphia	1,724,677.50
Union Passenger Railway Company of Philadelphia	1,416,879.10
West Philadelphia Passenger Railway Company	445,027.12
Peoples Passenger Railway Company Stock Trust Certificates	1,195,864.00
Hestonville, Mantua & Fairmount Passenger Railroad Company:	
Common	33,915.76
Preferred	74,609.70
Philadelphia Traction Company	6,728,000.00
Electric & Peoples Traction Stock Trust Certificates	4,980,365.73
Union Traction Company of Philadelphia	2,407,895.58
Darby, Media & Chester Street Railway Company	49,640.00
TOTAL	$31,973,597.78

Issued to holders of the following bonds:

Darby, Media and Chester Street Railway Company 4½% First Mortgage Bonds, due July 1, 1936	$396,400.00
Doylestown and Willow Grove Railway Company First Mortgage 4% Bonds, due June 1, 1960	200,000.00
TOTAL	$596,400.00
TOTAL	$32,569,997.78*

*In addition to the Consolidated Mortgage Bonds to be issued in exchange for stock and/or stock trust certificates of Lessor Companies, and in addition to the Consolidated Mortgage Bonds to be issued in refunding certain outstanding bonds of Lessor Companies, as set forth above, there will also be issued: (1) to the Trustee of $523,000 face amount of Union Traction Company of Philadelphia 4% Sinking Fund Collateral Trust Mortgage Bonds due July 1, 1952, outstanding, in exchange for the existing collateral security therefor, $2,333,400 face amount of the aforesaid 3%-6% Consolidated Mortgage Bonds of Transportation Company; and (2) to the Trustee of $2,107,000 face amount of Philadelphia Rapid Transit Company 5% Collateral Bonds due February 1, 1957 outstanding, in exchange for the existing collateral security therefor, $9,476,700 face amount of said 3%-6% Consolidated Mortgage Bonds. These said additional Consolidated Mortgage Bonds, which will be in the total face amount of $11,810,100, will be owned by Transportation Company and not outstanding in the hands of the public but held by the Trustees for the aforesaid collateral trust bonds as collateral security therefor; the said two respective amounts of said Consolidated Mortgage Bonds are in such amount that the fixed interest thereon would equal the interest and sinking fund payments required by the indentures under which the aforesaid respective collateral trust bonds were issued. Such Consolidated Mortgage Bonds shall be cancelled upon the retirement of the said respective obligations which they will secure.

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EXHIBIT 6-F: FORM OF CONSOLIDATED MORTGAGE BOND AND COUPONS.

(Form of Bond)

$100 $100

PHILADELPHIA TRANSPORTATION COMPANY

Consolidated Mortgage 3%-6%, Bond Series A
Due January 1, 2039

No. C00000 No. C00000

PHILADELPHIA TRANSPORTATION COMPANY hereinafter called the Company, a corporation of the Commonwealth of Pennsylvania, for value received, hereby promises to pay to bearer, or if this bond be registered as to principal to the registered holder hereof, on the first day of January, 2039, at the office of Fidelity-Philadelphia Trust Company in the City of Philadelphia, Commonwealth of Pennsylvania, or at the office in said city of any successor paying agent, or at the office of the paying agent of the Company in the Borough of Manhattan, The City and State of New York, the principal sum of One Hundred Dollars in such coin or currency of the United States of America as at the time of payment is legal tender for the payment of public and private debts, and to pay fixed interest on said principal sum at either of said offices in like coin or currency from January 1, 1939, until this bond shall be paid or the payment or redemption hereof duly provided for, at the rate of Three Per Cent. (3%) per annum, payable semi-annually on the said first days of January and July in each year, but only upon the presentation and surrender of the fixed interest coupons hereto annexed as they severally mature.

The Company further promises to pay for each year income interest to the extent to which net income is suf-

ficient up to Three Per Cent. (3%) per annum, in addition to the said fixed interest of Three Per Cent. (3%) per annum, the extent to which net income is sufficient for the payment of said income interest being determined from an annual income statement covering the twelve months ending December 31 of each year all as more particularly set forth in the indenture hereinafter referred to. Notice of the amount of such income interest for each preceding year will be given by the Company to the Trustee on or before May 1 of each year and the said income interest is payable, at either of said offices, in such coin or currency of the United States of America as at the time of payment is legal tender for the payment of public and private debts, annually on the first day of July in each year, but only upon the presentation and surrender of the income interest coupons hereto annexed as they severally mature. Said income interest is non-cumulative and shall be paid only for the years in which net income is sufficient therefor.

Principal of this bond and interest hereon are payable without deduction for any personal property taxes or corporate loans taxes that may be imposed by the Commonwealth of Pennsylvania up to but not exceeding five mills per annum in the aggregate on each dollar of the principal amount hereof which the Company or any officer thereof or the Trustee hereinafter referred to may be required to pay thereon, or to deduct or retain therefrom under any present or future law of the Commonwealth of Pennsylvania.

The Company reserves the right to require the holder of this bond or of any coupon detached herefrom, in connection with the payment of this bond or of such coupon, to present to Fidelity-Philadelphia Trust Company or any successor or other paying agent a certificate, in such form as the Company may from time to time prescribe, to enable it to determine its duties and liabilities with respect

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to any taxes, assessments or governmental charges which it may be required to deduct or withhold therefrom under any present or future law of the United States of America or of any state, county, municipality or taxing authority therein and giving, among other information, the identity and residence of the owner or holder of this bond or of such coupon; and the Company shall be entitled to determine its duties and liabilities with respect to such deduction or withholding on the basis of the information contained in such certificate or, if no such certificate shall be so presented on the basis of any presumption created by any such law, and shall be entitled to act in accordance with such determination.

This bond is one of a series of bonds, in both coupon form with interest coupons attached and fully registered form without interest coupons, designated as Consolidated Mortgage 3%-6% Bonds Series A due January 1, 2039. The bonds of the said series are part of an issue of bonds of the Company authorized under and pursuant to and all secured by an indenture of mortgage, or deed of trust, dated as of January 1, 1939, (hereinafter referred to as the indenture), duly executed and delivered by the Company to Fidelity-Philadelphia Trust Company as Trustee, to which indenture, including all indentures supplemental thereto, reference is hereby made for a description of the property mortgaged, the nature and extent of the security and the rights and limitations of rights thereunder of the holders of the said bonds and coupons and of the Company and the rights, duties and immunities thereunder of the Trustee. No bondholder or bondholders shall be entitled to institute any action, suit or any proceedings whatsoever for the enforcement of said indenture, or any right thereunder, except as therein provided. The said bonds are issuable in successive series, which may vary as to date, date of maturity, rate of interest and in other ways in the said indenture provided.

44a *Form of Consolidated Mortgage Bond and Coupons.*

This bond is subject to redemption at any time upon notice published once a week for at least four (4) consecutive weeks in a daily newspaper printed in the English language and published and of general circulation in the Borough of Manhattan, The City and State of New York and in a similar newspaper published and of general circulation in the City of Philadelphia, Commonwealth of Pennsylvania, the first publication to be at least thirty (30) days prior to the date fixed for redemption, as provided in the indenture, by payment of the principal amount hereof with accrued fixed interest to the date fixed for redemption and by payment of a further sum equal to interest at the maximum income interest rate of Three Per Cent. (3%) per annum to the date fixed for redemption from the end of the last calendar year for which income interest has been paid or would, at the date fixed for redemption, have been paid, if earned.

This bond is entitled to the benefits and security of a Sinking Fund as provided in said indenture.

In case of default as defined in said indenture, the principal of all bonds secured by said indenture may be declared due and payable in the manner and with the effect provided in said indenture.

This bond shall pass by delivery unless registered as to the principal hereof in the holder's name at the office of the Trustee in the City of Philadelphia, Commonwealth of Pennsylvania, or at the office in said city of any successor agent of the Company for such purpose or at the office of an agent of the Company appointed for such purpose in the Borough of Manhattan, The City and State of New York, such registry being noted on the bond by the agent of the Company for such purpose, after which no transfers shall be valid unless made in either of such offices by the registered holder in person or by his attorney duly authorized in writing and similarly noted on the bond; but thereafter this bond may be discharged

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from registration by being transferred in like manner to bearer and thereupon transferability by delivery shall be restored, and it may again from time to time be registered or transferred to bearer as before. No such registration, however, shall affect the negotiability of the interest coupons hereto annexed, which shall continue to be payable to bearer and transferable by delivery merely and the payment thereof to bearer shall fully discharge the Company in respect of the interest therein mentioned, whether or not this bond be registered.

The coupon bonds of this Series A are issuable in the denominations of One Hundred Dollars ($100.), Five Hundred Dollars ($500.) and One Thousand Dollars ($1,000.). Coupon bonds of this Series A totalling Five Hundred Dollars ($500.) in principal amount may be exchanged for a coupon bond of this Series A in the principal amount of Five Hundred Dollars ($500.), and coupon bonds of this Series A totalling One Thousand Dollars ($1,000.), in principal amount may be exchanged for a coupon bond of this Series A in the principal amount of One Thousand Dollars ($1,000.) upon surrender for cancellation of the bonds to be so exchanged with all unmatured coupons attached. The registered bonds without coupons of this Series A are issuable in multiples of One Thousand Dollars ($1,000.) in such denominations as the Company may determine, but in no event in denominations of less than Ten Thousand Dollars ($10,000.). Except in the case of a bond drawn for redemption, the coupon bonds and the registered bonds without coupons are interchangeable in authorized denominations and like principal amounts; and in and by the indenture it is covenanted that upon payment of the charges and otherwise as provided therein, any such interchange may be made by the holder of any bond or bonds upon presentation thereof for that purpose at the office of the Trustee, in the City of Philadelphia, Commonwealth of Pennsylvania, or at the office in said

city of any successor agent of the Company for such purpose, or at the office of an agent of the Company appointed for such purpose in the Borough of Manhattan, The City and State of New York.

This bond is issued, delivered, and intended to circulate as a negotiable instrument, unless registered. Each successive holder or owner hereof, or of any interest coupon appertaining hereto by accepting the same, shall be deemed to have agreed that this bond, unless registered, and the coupons hereto appertaining, whether or not this bond be registered, shall be construed as negotiable instruments; that every holder's or owner's rights, risks and remedies in respect to this bond, unless registered, and in respect to the interest coupons hereto appertaining, whether or not this bond be registered, shall be those of holders or owners of negotiable instruments; that the Company and the Trustee may deem and treat the bearer of this bond, if not registered, and if registered, the registered holder hereof, and the bearer of the interest coupons appertaining to this bond, whether or not this bond be registered, as the absolute owner hereof or thereof for all purposes, and shall not be affected by any notice to the contrary; and that the purchaser, for value and without notice of prior equities, of this bond, unless registered, or of any coupon hereto appertaining, whether or not this bond is registered shall be and become the absolute owner of this bond or of such coupon, unaffected by any rights or equities of any previous holder or owner hereof or thereof.

No recourse shall be had for the payment of the principal of this bond, or interest hereon, or for any claim based hereon, or in respect hereof, or of said indenture against any stockholder, officer or director of any constituent corporation merged and consolidated into the Company, or any past, present or future stockholder, officer or director of the Company or of any successor

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corporation as such, either directly or through the Company or through a receiver or trustee, whether by virtue of any constitution, statute or rule of law, or by the enforcement of any assessment or penalty or otherwise, all such liability being by the acceptance hereof and as part of the consideration for the issue hereof, expressly released.

This bond shall not become valid or obligatory for any purpose until it shall have been authenticated by the execution of the certificate hereon endorsed by the Trustee under the said indenture.

In Witness Whereof Philadelphia Transportation Company has caused this bond to be signed in its corporate name by its President, or one of its Vice-Presidents, and its corporate seal, or a facsimile thereof, to be hereunto affixed and attested by its Secretary or one of its Assistant Secretaries, and coupons for fixed interest and for income interest bearing the facsimile signature of its Treasurer to be attached hereto as of the first day of January, A. D. 1939.

PHILADELPHIA TRANSPORTATION COMPANY,
By

President.

[SEAL]
Attest:

Secretary.

Any United States documentary stamps required by law in connection with the issuance of this bond have been or will be affixed to the within-mentioned Indenture and duly cancelled.

48a *Form of Consolidated Mortgage Bond and Coupons.*

(Form of Fixed Interest Coupon)

On the first day of July 1939 (unless the bond below mentioned shall have been called for previous redemption and payment duly provided for), PHILADELPHIA TRANSPORTATION COMPANY, for value received, will pay to the bearer, on surrender of this coupon, at the office of Fidelity-Philadelphia Trust Company in the City of Philadelphia, Commonwealth of Pennsylvania, or at the office in said city of any successor paying agent, or at the office of the paying agent of the Company in the Borough of Manhattan, the City and State of New York, One and 50/100 Dollars ($1.50) in such coin or currency of the United States of America as at the time of payment is legal tender for the payment of public and private debts, without deduction for Pennsylvania personal property or corporate loans taxes up to but not exceeding five mills per annum in the aggregate on each dollar of the principal amount of the bond to which this coupon is attached, being six months' fixed interest then due on its consolidated mortgage 3%-6% Bond Series A due January 1, 2039.

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GEORGE W. DAVIS,
Treasurer.

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Form of Consolidated Mortgage Bond and Coupons. 49a

(Form of Income Interest Coupon)

On the first day of July 1940 (unless the bond below mentioned shall have been called for previous redemption and payment duly provided for), PHILADELPHIA TRANSPORTATION COMPANY, for value received, will pay to the bearer, on surrender of this coupon, at the office of Fidelity-Philadelphia Trust Company, in the City of Philadelphia, Commonwealth of Pennsylvania, or at the office in said city of any successor paying agent, or at the office of a paying agent of the Company in the Borough of Manhattan, the City and State of New York, the amount of income interest, if any, payable for the year ending, December 31 next preceding said July 31 in accordance with the Bond to which this coupon is attached, in such coin or currency of the United States of America as at the time of payment is legal tender for the payment of public and private debts, without deduction for Pennsylvania personal property or corporate loans taxes up to but not exceeding five mills per annum in the aggregate on each dollar of the principal amount of said Bond, being consolidated mortgage 3%-6% Bond Series A due January 1, 2039.

No. C 00000

GEORGE W. DAVIS,
Treasurer.

PETITIONER'S EXHIBIT 15: LETTER RULING OF OCTOBER 9, 1940 FROM DEPUTY COMMISSIONER.

TREASURY DEPARTMENT

Washington

[Seal]

Office of
Commissioner of Internal Revenue

Address Reply to
Commissioner of Internal Revenue
and Refer to

IT:P:T:2 Oct 9-1940
RLB

Pennsylvania Transportation Company,
Mitten Building,
Philadelphia, Pennsylvania.

Attention: H. Renner, Jr.,
Assistant Comptroller.

Sirs:

Further reference is made to your letter of September 23, 1940, and accompanying copy of the Second Revised Plan of Reorganization of your company left in the Bureau by H. Renner, Jr., Assistant Comptroller, on September 24, 1940.

Mr. Renner has requested a specific ruling with regard to the treatment, for the purposes of the Federal income tax, of the amounts paid by your company as interest on its Consolidated Mortgage Bonds, the filing of ownership certificates on form 1012 with respect to such interest payments, and the withholding of tax at the source with regard to the interest payments made to nonresident alien bondholders.

It is the contention of Mr. Renner that since your company did not exist as a separate taxable entity prior to January 1, 1940, although the Plan of Reorganization

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of December 1, 1937, as amended June 1, 1938 and November 15, 1938, under which it commenced operations provided for the payment of interest on the Consolidated Bonds as of January 1, 1939, the amounts paid in January 1940 should not be regarded as "true interest" on indebtedness.

The authorized capitalization of your company consists, in part, of the Consolidated Mortgage Bonds secured by a mortgage and deed of trust, junior to the deed of trust and mortgage securing the first and refunding mortgage bonds. The Consolidated Bonds were issued in exchange for stock and/or stock trust certificates of lessor companies outstanding in the hands of the public. All of these bonds are of a single series dated January 1, 1939, and mature on January 1, 2039, bear a fixed interest at the rate of 3 percent per annum and, under certain conditions mentioned in the Plan of Reorganization additional interest may be paid at the rate of 3 percent per annum. (Section 3(b) of the Plan of Reorganization as revised.)

The gross amount representing the interest payment made in January 1940 was not taken into consideration in the Plan of Reorganization, as revised, which was determined by this office to be a nontaxable transaction.

Gross income as defined in section 22(a) of the Internal Revenue Code includes interest. The fact that a corporate entity was not actually in existence as of the accrual date of interest on an outstanding obligation does not change the character of the income. The distribution under consideration in the instant case is held to represent a payment of interest on an outstanding obligation. Accordingly, as the payments made in January 1940 represent payments of interest, ownership certificates are required with respect to such payments. Furthermore, tax at the prescribed rate must be deducted and withheld from all payments of interest made to nonresident alien bondholders. (Section 143(b) of the

52a *Letter Ruling of October 9, 1940 from Deputy Commissioner.*

Internal Revenue Code and section 143(b) of the Internal Revenue Code, as amended.)

Respectfully,

TIMOTHY C. MOONEY,
Deputy Commissioner,

By
L. K. SUNDERLIN
Chief of Section.

TREASURY DEPARTMENT

Washington

[Seal]

Office of
Commissioner of Internal Revenue

Address Reply to
Commissioner of Internal Revenue
and Refer to

IT:P:T:2
RLB

Oct 14 1940

Philadelphia Transportation Company,
Mitten Building,
Philadelphia, Pennsylvania.

Attention: H. Renner, Jr.,
Assistant Comptroller.

Sirs:

Your attention is invited to the fact that in Bureau letter of October 9, 1940, your company was addressed in the name of Pennsylvania Transportation Company instead of Philadelphia Transportation Company. A conformed carbon copy with your name and address properly shown is attached.

Respectfully,

TIMOTHY C. MOONEY,
Deputy Commissioner.

By
L. K. SUNDERLIN
Chief of Section.

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Letter Ruling of October 9, 1940 from Deputy Commissioner. 53a

IT:P:T:2
RLB

October 9, 1940.

Philadelphia Transportation Company,
Mitten Building,
Philadelphia, Pennsylvania.

Attenion: H. Renner, Jr.,
Assistant Comptroller.

Sirs:

Further reference is made to your letter of September 23, 1940, and accompanying copy of the Second Revised Plan of Reorganization of your company left in the Bureau by H. Renner, Jr., Assistant Comptroller, on September 24, 1940.

Mr. Renner has requested a specific ruling with regard to the treatment, for the purposes of the Federal income tax, of the amounts paid by your company as interest on its Consolidated Mortgage Bonds, the filing of ownership certificates on form 1012 with respect to such interest payments, and the withholding of tax at the source with regard to the interest payments made to nonresident alien bondholders.

It is the contention of Mr. Renner that since your company did not exist as a separate taxable entity prior to January 1, 1940, although the Plan of Reorganization of December 1, 1937, as amended June 1, 1938 and November 15, 1938, under which it commenced operations provided for the payment of interest on the Consolidated Bonds as of January 1, 1939, the amounts paid in January 1940 should not be regarded as "true interest" on indebtedness.

The authorized capitalization of your company consists, in part, of the Consolidated Mortgage Bonds secured by a mortgage and deed of trust, junior to the deed of trust and mortgage securing the first and refunding mort-

gage bonds. The Consolidated Bonds were issued in exchange for stock and/or stock trust certificates of lessor companies outstanding in the hands of the public. All of these bonds are of a single series dated January 1, 1939, and mature on January 1, 2039, bear a fixed interest at the rate of 3 percent per annum and under certain conditions mentioned in the Plan of Reorganization additional interest may be paid at the rate of 3 percent per annum. (Section 3(b) of the Plan of Reorganization as revised.)

The gross amount representing the interest payment made in January 1940 was not taken into consideration in the Plan of Reorganization, as revised, which was determined by this office to be a nontaxable transaction.

Gross income as defined in section 22(a) of the Internal Revenue Code includes interest. The fact that a corporate entity was not actually in existence as of the accrual date of interest on an outstanding obligation does not change the character of the income. The distribution under consideration in the instant case is held to represent a payment of interest on an outstanding obligation. Accordingly, as the payments made in January 1940 represent payments of interest, ownership certificates are required with respect to such payments. Furthermore, tax at the prescribed rate must be deducted and withheld from all payments of interest made to non resident alien bondholders. (Section 143(b) of the Internal Revenue Code and section 143(b) of the Internal Revenue Code, as amended.)

Respectfully,

TIMOTHY C. MOONEY,
Deputy Commissioner.

By
(Signed) L. K. SUNDERLIN
Chief of Section.

RLB/AJ-2(KSP)

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PETITIONER'S EXHIBIT 16: LETTER OF JANUARY 19, 1943 FROM INTERNAL REVENUE AGENT IN CHARGE ACCEPTING 1940 INCOME TAX RETURN.

TREASURY DEPARTMENT

Internal Revenue Service

[Seal]
Office of
Internal Revenue Agent in Charge
..... Division

January 19, 1943.

Philadelphia Transportation Co.
Mitten Building
Broad & Locust Streets
Philadelphia, Pa.

In re: Income Tax Return
Year(s) covered: 1940

Upon examination of your income tax return(s) for the year(s) indicated above, the conclusion has been reached that it (they) should be accepted as filed.

I am sure you will appreciate that should subsequent information be received which would materially change the amount reported, it will be necessary under existing laws to redetermine your tax liability.

Respectfully,

(signed) R. T. MILES
Internal Revenue Agent in Charge.

Form 850-C
Revised May 1942
FFR

U. S. Government Printing Office 16-8569-1

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UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

No. 9772

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

PHILADELPHIA TRANSPORTATION COMPANY, RESPONDENT

On Petition for Review of the Decision of the Tax Court of the United States

Argued February 23, 1949

Before GOODRICH, WALLER, and MCLAUGHLIN, Circuit Judges

OPINION OF THE COURT

(Filed March 21, 1949)

By GOODRICH, Circuit Judge.

The Philadelphia Transportation Co., the taxpayer here, was formed on January 1, 1940 as the culmination of reorganization proceedings involving 65 corporations concerned in Philadelphia's public transportation system. In accordance with the reorganization plan, the taxpayer issued, in January, 1940, mortgage bonds dated January 1, 1939 and bearing interest from that date. The interest coupons for 1939 and 1940 were redeemed by the taxpayer in 1940, as required by the reorganization plan.

The taxpayer computes its tax liability on an accrual basis. In its income tax return for 1940, it claimed a deduction for the 1939 and 1940 coupons as "interest accrued" in 1940.[1]

These basic facts raise the crucial question, the answer to which will dispose of the case. Was the interest allocated as 1939 interest properly deducted from the taxpayer's 1940 income as interest accrued in 1940? The Tax Court held that it was. In this appeal, the Commissioner seeks reversal on three principal grounds. He argues, first, that the amount deducted was not interest. It was not interest, he says, because interest is compensation for the use of money, and the taxpayer held no money,

[1] The applicable section of the Internal Revenue Code, § 23 (b), provides:
"Sec. 23. Deductions from Gross Income. In computing net income there shall be allowed as deductions:
* * * * *
(b) Interest.—All interest paid or accrued within the taxable year on indebtedness * * *." 26 U. S. C. A. § 23 (b).

borrowed or otherwise, in 1939. The Commissioner looks for support on this point to the statutory language which refers to "interest accrued on indebtedness." He concludes that without indebtedness in 1939, there could have been no interest. And there was no indebtedness in 1939, he says, because the taxpayer had no corporate existence then.

The Commissioner's second point is that the taxpayer really took over the obligation to pay 1939 interest as a part of the cost of the assets acquired in the reorganization. We discuss this point below. And finally the Commissioner argues that even if the amount in question be treated as interest, a deduction of interest for more than the current year may not be made from that year's income.

The point last stated is easily answered. No provision of the Internal Revenue Code prohibits such a deduction. Section 43 of the Code, 26 U. S. C. A. § 43, provides that "the liabilities of one year cannot be used to reduce the income of a subsequent year." It is upon this provision that the Commissioner relies. But the issue is whether the item in question here is a liability of the year 1940. If it accrued in 1940, it is deductible in 1940 and in no other year, whether or not it is based on transactions allocated for other purposes to other periods. One decision specifically supports the deduction of 2 years' interest in one year in a proper case,[2] and three other decisions, including one from this Court, support the proposition in principle.[3]

We turn, then, to the Commissioner's first two arguments. We think that the fog surrounding the no debt-no interest contention is best cleared by a simply hypothetical illustration. A corporation is formed in 1940. It is brand new and without corporate forbears. It issues in 1940 a series of 20-year coupon bonds. For reasons best known to the management, it is decided to date the bonds as of January 1, 1939 to mature January 1, 1959, and to redeem the first two interest coupons in 1940. The corporation pays its taxes on an accrual basis. Can there be any doubt that the interest accrued on the two coupons in 1940 and was properly deductible in that year? We think that in the hypothetical case the situation is the same as if the 1940 interest coupons were just double the later ones in amount. There was indebtedness in 1940, interest accrued on that indebtedness in 1940, and we think it is chargeable for tax purposes, as well as bookkeeping purposes, for that year.

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[2] Oregon Pulp & Paper Co. v. Commissioner, 47 BTA 722 (1942), petition for review dismissed (C. C. A. 9, November 2, 1943).

[3] Commissioner v. Pressed Steel Car Co., Inc., 152 F. 2d 280 (C. C. A. 3, 1945); Ernst Kern Co. v. Commissioner, 1 T. C. 249 (1942); Columbia River Paper Mills v. Commissioner, 43 BTA 104 (1940), aff'd 126 F. 2d 2009 (C. C. A. 9, 1942). It is true that our decision was made at a time when the Dobson case blinders prevented the judicial eye from roving over the record. We think the result was right though, perforce, compelled.

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We think the present case is similar to the hypothetical one in all respects except that the taxpayer was the product of a reorganization and came into existence with the obligation to pay fixed and variable interest on the bonds it was to issue to the shareholders of its corporate predecessors. These added factors do not, in our judgment, alter the result. The taxpayer, as a new corporation, created its own new indebtedness. It did not assume existing liabilities on which interest had already accrued against predecessor companies. If it had, there would be merit in the Commisisoner's point that the obligation was part of the cost of the asests acquired by the taxpayer.[4]

But that is not the fact. No obligation was owed by the predecessor companies to their shareholders except insofar as assets might have remained for distribution to them when corporate affairs were wound up. Moreover, neither the present taxpayer nor any of its predecessors was in a position to take advantage of a 1939 deduction for the interest payments in question. As our brethren in the Ninth Circuit said in Commissioner v. Columbiæ River Paper Mills, 126 F. 2d 1009, 1010 (C. C. A. 9, 1942): "The arrangement was a logical one under the circumstances, * * * It is not suggested that there was any purpose of tax avoidance * * *." We conclude, therefore, as we did in Pressed Steel Car Co. v. Commissioner, 152 F. 2d 280 (C. C. A. 3, 1946), that the Tax Court correctly decided that the amount in dispute represented accrued interest within the meaning of Section 23 (b) of the Internal Revenue Code.[5]

The decision of the Tax Court will be affirmed.

WALLER, Circuit Judge, dissenting: It is with regret that I cannot bring myself in line with the excellent opinion of the majority in this case. I cannot escape the force of innumerable opinions of courts throughout the country holding that interest is the premium paid for the use of money, or—as held by the Supreme Court in Deputy Administratrix v. Dupont, 308 U. S. 488 (text 497)—that interest "is the amount which one has contracted to pay for the use of borrowed money."

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[4] Cases in which the indebtedness was that of the taxpayer's vendor or predecessor, and was taken over by the taxpayer with the obligation to pay interest already accrued, have been properly treated as capital transactions. Commissioner v. Breyer, 151 F. 2d 267, 272 (C. C. A. 3, 1945); Rodney v. Commissioner, 145 F. 2d 692 (C. C. A. 2, 1944); Pratt-Mallory Co. v. United States, 12 F. Supp. 1020, 1023 (Ct. Cl. 1936). Cases like Lloyd v. Commissioner, 154 F. 2d 643 (C. C. A. 3, 1946), in which the proceeds of the sale of unmatured interest coupons by a banking syndicate which was not the obligor were held improperly declared as a deduction for payment of "interest," are clearly without application to the present case.

[5] All the authorities on this point have reached the same result, with one exception. Commissioner v. Pressed Steel Car Co., Inc., 152 F. 2d 280 (C. C. A. 3, 1945); Ernst Kern Co. v. Commissioner, 1 T. C. 249 (1942); Columbia River Paper Mills v. Commissioner, 43 BTA 104 (1940), aff'd 126 F. 2d 1009 (C. C. A. 9, 1942); Oregon Pulp & Paper Co. v. Commissioner, 47 BTA 722 (1942), petition for review dismissed (C. C. A. 9, November 2, 1943). Contra: Commissioner v. Drovers Journal Publishing Co., 135 F. 2d 276 (C. C. A. 7, 1943).

In 1939 the taxpayer here borrowed no money, acquired no property, used no money or property of others, and owed no debts to which interest could have been an incident. On the contrary it was not in existence until January 1, 1940, and neither made, nor could have made, any contract prior to its coming into being. It, doubtless, could have ratified, upon its organization, lawful contracts theretofore made by its promoters, but the procedure adopted was not that of ratifying a prior contract made by its promoters but of making its own contract whereby it sought to engage in the Canutian pastime of turning back the tide for one year and thus to pay interest on money which it never used nor borrowed in 1939, but with which it purchased property in 1940.

The bonds were issued for the acquisition of the assets of the sixty-five affiliated companies. The consideration for the purchase of such assets was the execution and delivery of bonds and interest coupons thus antedated. Before its organization no assets were delivered to it, no money advanced, no forbearance extended. In short, bonds with one year's unearned and unaccrued interest coupons were delivered in consideration for the sale of such assets.

It seems clear that the payment represented by the 1939 coupons was not a payment of "interest" but was merely a part of the consideration for the acquisition of the assets acquired in part therewith, and as such was a capital investment rather than rent for the use of money or its equivalent.

A true Copy:
Teste:

Clerk of the United States Court of Appeals
for the Third Circuit.

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United States Court of Appeals for the Third Circuit

No. 9772

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

PHILADELPHIA TRANSPORTATION COMPANY, RESPONDENT

On Petition To Review a Decision of the Tax Court of the United States

Present: GOODRICH, WALLER, and MCLAUGHLIN, Circuit Judges

JUDGMENT

This cause came on to be heard on the record from the Tax Court of the United States, and was argued by counsel.

On consideration whereof, it is now here ordered, adjudged and decreed by this Court that the decision of the said Tax Court in this cause be, and the same is hereby affirmed.

For the Court,

HERBERT F. GOODRICH,
Circuit Judge.

MARCH 21, 1949.

Endorsements—

Judgment Affirming Decision of the Tax Court.

Received and filed Mar. 21, 1949. Ida O. Creskoff, Clerk.

I, Ida O. Creskoff, Clerk of the United States Court of Appeals for the Third Circuit, do hereby certify the foregoing to be a true and faithful copy of the original Appendix to Petitioner's Brief, Appendix to Respondent's Brief, and proceedings in this Court in the case of Commissioner of Internal Revenue, Petitioner vs. Philadelphia Transportation Company, Respondent, No. 9772, on file, and now remaining among the records of the said Court, in my office.

In testimony whereof, I have hereunto subscribed my name and affixed the seal of the said Court, at Philadelphia, this 12th day of May in the year of our Lord one thousand nine hundred and forty-nine, and of the Independence of the United States the one hundred and seventy-third.

[SEAL]

(S) IDA O. CRESKOFF,
Clerk of the U. S. Court of Appeals, Third Circuit.

U. S. GOVERNMENT PRINTING OFFICE: 1949

Supreme Court of the United States

No. 126, October Term, 1949

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

PHILADELPHIA TRANSPORTATION COMPANY

Order allowing certiorari

Filed October 10, 1949

The petition herein for a writ of certiorari to the United States Court of Appeals for the Third Circuit is granted. The case is transferred to the summary docket.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

861430—49——2 U. S. GOVERNMENT PRINTING OFFICE: 1949